Melrose
Buy
Improve
Sell

Melrose Industries PLC

Annual Report 2020

Melrose Industries PLC

Acquiring good quality manufacturing businesses, making operational improvements, realising shareholder value at the appropriate time and then returning this value to shareholders, continue to be the fundamentals of the "Buy, Improve, Sell" business strategy that Melrose has followed since being founded in 2003.

01 Strategic Report

88 Governance

128 Financial statements

208 Shareholder information

For more information visit **melroseplc.net**

Cautionary statement

Annual Report 2020

"Whilst the COVID-19 crisis has had a major detrimental effect this year, Melrose has generated record cash flows and continued to invest to improve our businesses. All of this positions the Group well for a good recovery and strong performance in the future."

Justin Dowley
Non-executive Chairman

For more information about our successful history of shareholder value creation
See pages 4 to 5

Highlights for 2020

Headline figures

6% (1)

Increase in adjusted free cash flow(2).

£628m

Adjusted free cash flow(2).

over 80%

Reduction in the accounting deficit on the GKN UK defined benefit pension schemes since acquisition(3).

£270m

Of cash contributions to the GKN UK defined benefit pension schemes from the Group so far during Melrose ownership, making them significantly better funded.

167%

Adjusted operating cash flow conversion (pre-capex)(4).

0.75 pence per share

Final dividend.

11%

Reduction in GHG emissions produced by the Group's facilities in 2020 versus 2019.

(1) Calculated compared to 2019 annualised adjusted free cash flow. Described in the glossary to the financial statements on pages 204 to 207.
(2) Adjusted free cash flow excludes restructuring spend and in 2019 one-off payments to deferred benefit pension schemes. Described in the glossary to the financial statements on pages 204 to 207.
(3) £0.7bn just before acquisition to £0.1bn in these results.
(4) Described in the glossary to the financial statements on pages 204 to 207.

Group revenue and operating profit

Adjusted(4) revenue

£9.4bn

Statutory revenue

£8.8bn

Adjusted(4) operating profit

£340m

Statutory operating loss

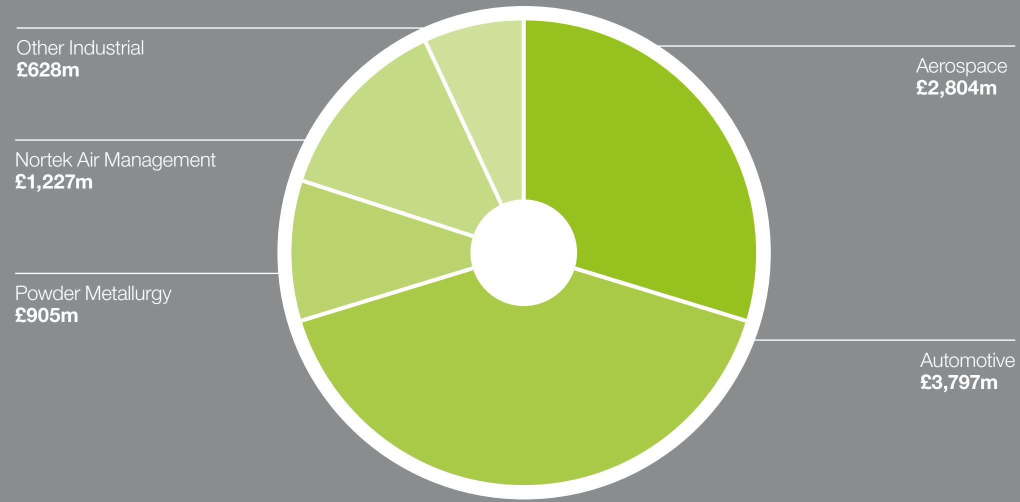
£338m

Divisional performance summary results
(for the year ended 31 December 2020)

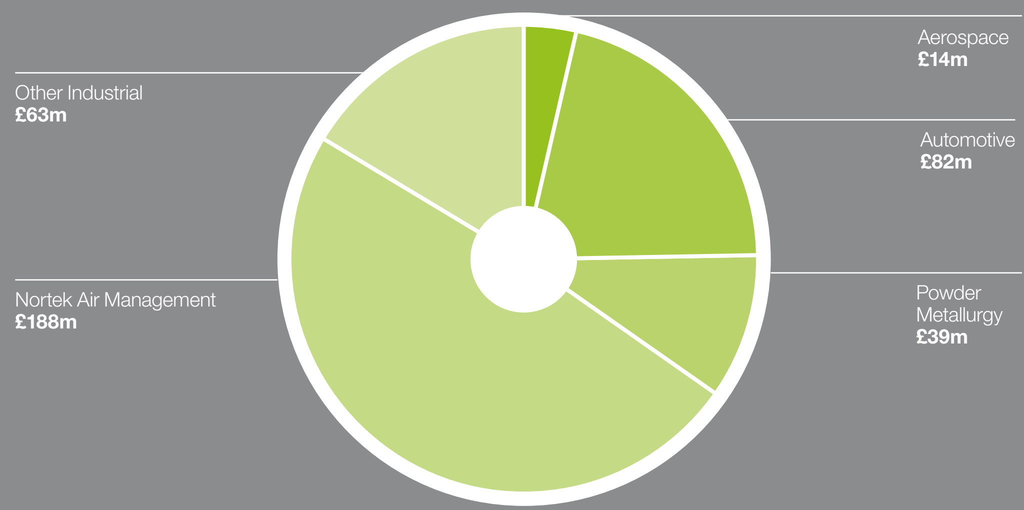
	Adjusted(1) revenue £m	Adjusted(1) operating profit/(loss) £m	Statutory revenue £m	Statutory operating profit/(loss) £m
Aerospace	2,804	14	2,798	(410)
Automotive	3,797	82	3,231	(183)
Powder Metallurgy	905	39	886	(57)
Nortek Air Management	1,227	188	1,227	149
Other Industrial	628	63	628	34
Corporate	–	(46)	–	129

(1) Described in the glossary to the financial statements on pages 204 to 207.

Adjusted(1) revenue £m



Adjusted(1) operating profit £m



Shareholder value creation

Since making its first acquisition in 2005, Melrose has achieved an average return on equity investment of 21%, with an increase in operating margins of between five and nine percentage points across businesses sold to date.

Melrose has delivered significant returns to shareholders since floating on AIM in 2003

Shareholder investment and gain (figures up to 31 December 2020)

£4.7bn
Cash return to shareholders since establishment

2.6x
Average return on equity across all businesses sold

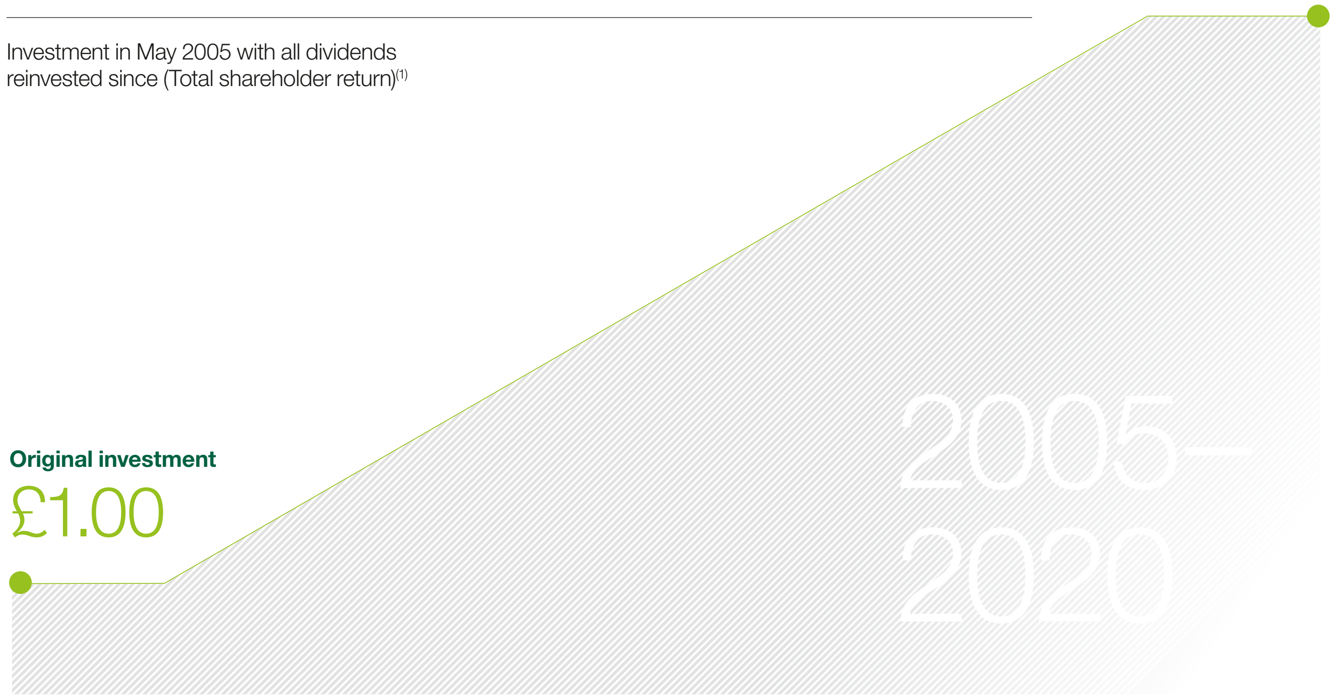
21%
Average annual return on equity investment since the first acquisition(1)

(1) Source: Datastream Total Shareholder Return Index.

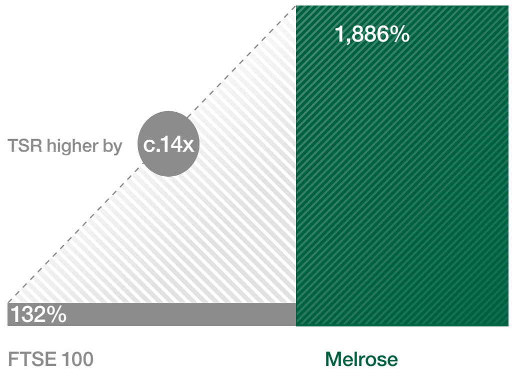
Track record for £1 invested in Melrose As at 31 December 2020

Investment in May 2005 with all dividends reinvested since (Total shareholder return)(1)

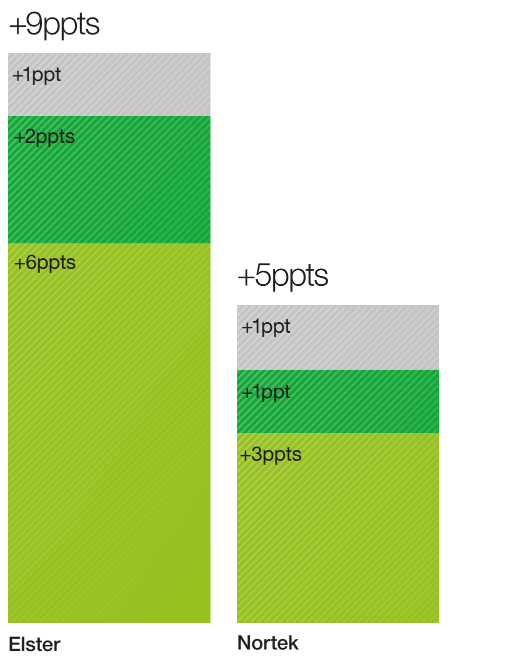
Gross return
£19.86
on original £1 investment



Total shareholder return (TSR)(1)(2)



How Elster and Nortek operating margin improved(3)



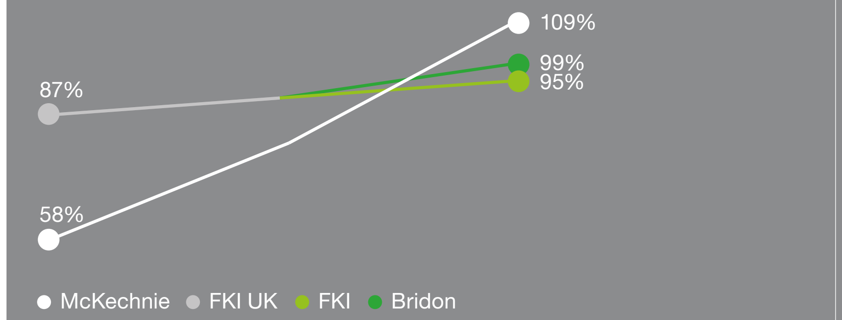
- Returns on capex and restructuring and other commercial actions.
- Central cost savings.
- Exit of low margin sales channels.

(1) Since Melrose's first acquisition (May 2005).
(2) Source: Datastream Total Shareholder Return Index.
(3) Nortek adjusted operating margin up to 31 December 2020.

Responsible approach to investing

Substantial improvements for all the UK pension schemes under ownership

Whilst under Melrose ownership, we improve contributions and provide better security to our businesses' pension schemes towards fully funded upon departure from the Group.

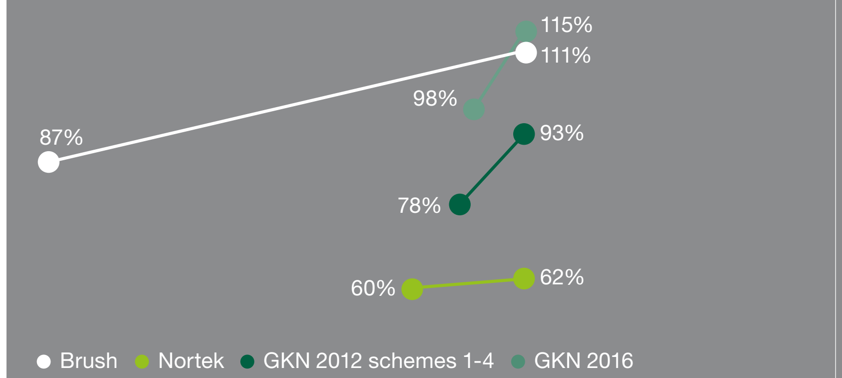


Responsible stewardship (figures up to 31 December 2020)

- For the GKN schemes, we were proactive, transparent and constructive in agreeing commitments with pension trustees during the acquisition of GKN. We committed to providing up to £1 billion of funding contributions; to doubling annual contributions to £60 million; making £150 million upfront contributions and further contributions on sales of business.

So far we have:

- Reduced the GKN UK defined benefit pension scheme accounting deficit by over 80% since just before acquisition through the doubling of annual contributions and significant one-off contributions.
- Applied more secure funding targets of Gilts +25 basis points (GKN 2016) and Gilts +75 basis points (GKN 2012 schemes 1-4) to achieve more prudent funding levels towards fully funded.
- Rebalanced the GKN schemes across the GKN division, to avoid overburdening any one business and to provide stability and better security for members.



Promoting strong Sustainability principles

This year we have enhanced our standalone Sustainability report (see pages 58 to 87), to highlight the investment, support and encouragement we provide to our businesses to enable them to pursue relevant improvements in relation to environmental, social and governance (ESG) matters.

c.£1bn
spent on research and development for Nortek, Elster and GKN acquisitions

Strategic Report

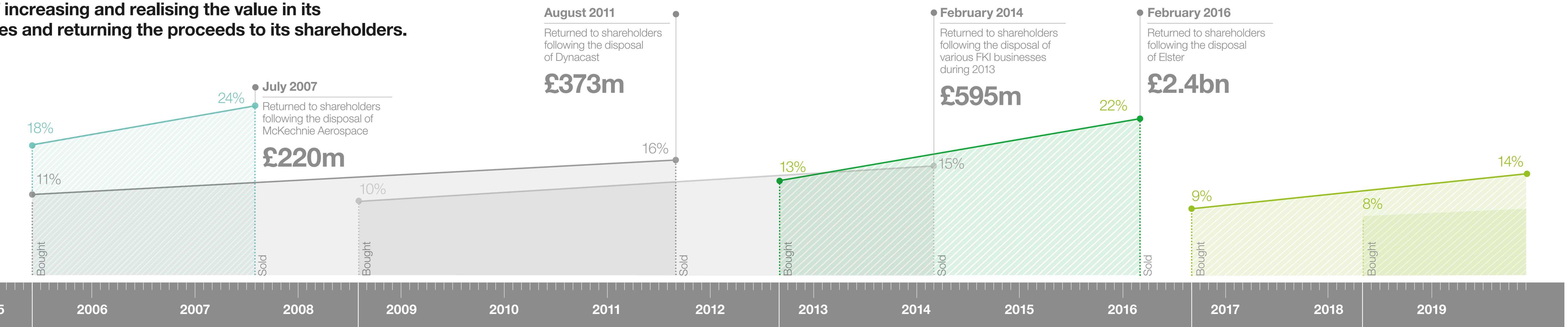
“Buy, Improve, Sell” – A history of success

Melrose continues to build on its 17-year track record of increasing and realising the value in its businesses and returning the proceeds to its shareholders.

Adjusted(1) operating margin improvement

Company	Entry	Current	Exit	Improvement	
McKechnie	18%	•	24%	>30%	+6ppts
Elster	13%	•	22%	>70%	+9ppts
Dynacast	11%	•	16%	>50%	+5ppts
FKI	10%	•	15%	>50%	+5ppts
Nortek	9%	14%	•	>50%	+5ppts

(1) Described in the glossary to the financial statements on pages 204 to 207.



Acquisition	May 2005	July 2008	August 2012	August 2016	April 2018

Company details

McKechnie/Dynacast

Bought for	£0.4bn
Equity raised on acquisition	£243m
Follow-on investment	£124m
Sold for	£0.8bn
Investment in business	51%
Equity rate of return	30%
Cash generated during ownership	£934m

Shareholder return on original equity: 3.0x

Commentary

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

Dynacast was a global provider of precision die cast components for a wide variety of industries. During our ownership we improved operating margins from 11% to 16% by successfully aligning capacity with customers and installing a success-driven organisational culture.

Overall we generated over £700 million in net cash proceeds from the businesses versus an equity investment of approximately £240 million, resulting in a return of 3.0x on shareholders' investment. This includes direct returns to shareholders after disposals of £220 million in 2007 and £373 million in 2011.

FKI

Bought for	£1.0bn
Equity raised on acquisition	£499m
Follow-on investment	£391m
Sold for	£1.4bn(1)
Investment in business	78%
Equity rate of return	29%
Cash generated during ownership	£1.8bn(1)

Shareholder return on original equity: 2.6x

FKI comprised a number of diverse businesses, and our improvement initiatives were centred around refocusing the FKI conglomerate to allow each of its businesses to stand alone, and making necessary investments to strengthen their market positions. We improved operating margins from 10% to 15% under our ownership and have since sold all of the businesses with the exception of Brush, which for these purposes only we are valuing at £100 million.

Overall we generated over £1.3 billion in net cash proceeds from the businesses versus an equity investment of approximately £500 million, resulting in a return of 2.6x on shareholders' investment. This includes direct returns to shareholders after disposals of £595 million in 2014 and £200 million in 2015.

(1) Includes estimated value of business not yet sold.

Elster

Bought for	£1.8bn
Equity raised on acquisition	£1.2bn
Follow-on investment	£287m
Sold for	£3.3bn
Investment in business	25%
Equity rate of return	33%
Cash generated during ownership	£3.3bn

Shareholder return on original equity: 2.3x

Elster was a US publicly-listed German-based manufacturer of meters operating through three separate divisions with different markets and drivers (Gas, Electricity, Water).

Under our ownership we oversaw operating profit margins increase from 13% to 22%, representing a 70% improvement in just three years. This was achieved by focusing each business on performance, end markets, customers and operations. We significantly expanded on an optimisation programme announced by Elster before our acquisition and significantly exceeded expectations.

Overall we generated over £2.5 billion in net cash proceeds from Elster versus an equity investment of approximately £1.2 billion, resulting in a return of 2.3x on shareholders' investment. This includes direct returns to shareholders after a disposal of all three businesses to Honeywell for £3.3 billion in 2015.

Nortek

Bought for	£2.2bn
Equity raised on acquisition	£1.6bn
Follow-on investment(1)	£0.3bn
Investment as % of initial equity	21%
Cash generated during ownership	£709m

Upon our acquisition, Nortek was a global diversified group, manufacturing innovative air management, security, home automation and ergonomic and productivity solutions. Suffering from fragmented operations and operational underperformance, we identified a range of world-class product ranges and strong brands that were underperforming their potential, but which through further investment would become well placed to address emerging market needs.

Under Melrose ownership, each business has undergone a significant transformation, freed from the restrictions of the formerly centralised group structure, and propelled by material, targeted investment in research and development, and productivity improvements. Significant Melrose investment in cutting-edge technology has yielded particularly notable market-leading positions, particularly in the case of StatePoint Technology®, which is a key contributor to a record year for the Nortek Air Management businesses. Each business now has strong foundations for significant profitable growth, including a sophisticated operating footprint with multiple paths for further optimisation and operational scalability. Having embedded a culture of operational excellence and new product development, supported by experienced and committed management teams, and adaptable manufacturing and engineering competencies, we are excited about further significant growth opportunities within the dynamic end markets served by the Nortek businesses.

(1) Up to 31 December 2020.

GKN

Bought for	£8.3bn
Equity raised on acquisition	£6.8bn
Follow-on investment(1)	£1.7bn
Investment(1) as % of initial equity	25%
Cash generated during ownership	£291m

GKN, upon our acquisition, was a multinational group of businesses making predominantly aerospace and automotive components. Upon taking control we immediately set about decentralising the businesses, and refocusing them on profitable sales rather than solely on growth. The GKN businesses now make up three distinct divisions within Melrose: Aerospace, Automotive and Powder Metallurgy. See pages 14 to 25 to find out more about our progress in improving the GKN businesses so far, and our plans for 2021.

Melrose Industries PLC Annual Report 2020

Our purpose and strategy

Melrose was founded in 2003 to empower businesses to unlock their full potential for the collective benefit of stakeholders, whilst providing shareholders with a superior return on their investment.

We have achieved this through the implementation of our "Buy, Improve, Sell" strategy.

Buy

- Good manufacturing businesses whose performance can be improved.
- Use low (public market) leverage.
- Melrose management are substantial equity investors.

Improve

- Free management from bureaucratic central structures.
- Change management focus, incentivise well.
- Encourage and implement sustainable business practices.
- Set strategy and targets and sign off investments.
- Drive operational improvements and sustainable production.
- Invest in the business and support research and development, particularly sustainable products.
- Focus on profitability, sustainability, and operating cash generation – not growth for the sake of growth.
- Improve products and customer relationships.
- Engage closely and often with key external stakeholders.
- Invest in the workforce, closely monitor health and safety, and secure the financial health of workplace pension schemes.

Sell

- Commercially choose the right time to sell, often between three and five years, but flexible.
- Return value to shareholders from significant disposals.

Our business model

Inputs | Value creation | Outputs

Inputs

Industry expertise

Core management group has operated in the UK and the international manufacturing arena for over two decades.

Highly experienced management team

The current team founded Melrose in 2003 with a view to buying and improving underperforming businesses. Since then it has overseen transactions with a total market value of over £10 billion.

Strong track record

Melrose has generated significant financial returns for its shareholders, achieving an average return on equity of 2.6x across the businesses sold to date and returned over £4.7 billion of cash to shareholders.

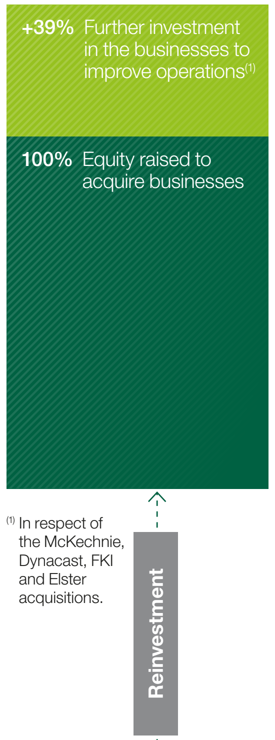
Operational efficiency

Our businesses benefit from substantial investment and changed management focus in order to drive growth. Melrose increased the operating margins of businesses sold by between five and nine percentage points.

Effective governance

The Board maintains high standards of corporate governance to ensure that Melrose achieves success for the benefit of the businesses we manage and our shareholders over the long term.

Follow-on investment during Melrose ownership for businesses sold



(1) In respect of the McKechnie, Dynacast, FKI and Elster acquisitions.

Value creation

Value creation model

Margin growth

Good but underperforming manufacturing businesses whose potential is unrealised.

Sales

Strong track record suggesting growth at least in line with their market.

Cash generation

A key focus is to make significant improvement to cashflows in the businesses we acquire.

Multiple expansion

Multiple expansion is never assumed, but has been achieved on all previous deals (on average +30%) as the businesses have been improved.

Businesses under improvement

Aerospace p.14

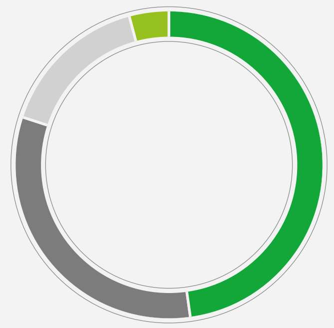
Automotive p.18

Powder Metallurgy p.22

Nortek Air Management p.26

Other Industrial p.30

How has Melrose created value?(1)



Margin improvement	48%
Multiple arbitrage	32%
Cash generation	16%
Sales growth	4%

(1) In respect of the McKechnie, Dynacast, FKI and Elster acquisitions.

Outputs

Shareholder investment and gain
(figures up to 31 December 2020):

Average return on equity across all businesses sold

2.6x

Cash return to shareholders since establishment

£4.7bn

Reinvestment

c.£1bn
Spent on research and development for Nortek, Elster and GKN acquisitions

Capital expenditure in 2020

£317m

Sustainability

The Melrose "Buy, Improve, Sell" model necessarily means that we inherit businesses that are underperforming in a number of different areas, including from a sustainability perspective.

The manufacturing businesses that we acquire often operate in the industries that are some of the most difficult to decarbonise. By the very nature of our model, (a) we provide the focus and investment that our businesses need to deliver significant financial returns and sustainability improvements; and (b) our Group sustainability performance and ratings will fluctuate during our investment cycle as we acquire new businesses in need of improvement, and sell businesses that we have improved.

Implementing Melrose Sustainability principles – our decentralised approach

We encourage, support and invest in our businesses to implement the following Melrose Sustainability principles and contribute to a sustainable future for the benefit of our stakeholders, as further detailed in our Sustainability report on pages 58 to 87:

- Respect and protect the environment.
- Promote diversity and prioritise and nurture the wellbeing and skills development of employees and the communities that they are part of.
- Exercise robust governance, risk management and compliance.
- Purposefully engage with key stakeholders to better understand and deliver on their expectations.

We invest in our businesses to bolster their research and development capabilities, to enable them to make products more sustainable and safer, with a focus on helping our businesses' customers and their wider industries to support the transition to a net zero carbon economy by 2050.

We encourage our businesses to champion the interests, safety and skills development of their employees.

We implement secure pension scheme funding, operational and financial best practice, and lead in promoting diversity.

We instil strong ethical values supported by high governance standards, through our Melrose Code of Ethics and Group policies, together with training and internal controls, which are supported by renewed management and governance structures.

We work with our businesses to set meaningful sustainability targets, alongside financial metrics, and we provide the investment to achieve them. We set a positive example for our businesses and provide them with a platform to share Group best practices and accelerate the pace of change within their organisations, whilst influencing positive change within our other businesses.

Sustained, positive Sustainability performance

The success of our "Buy, Improve, Sell" model relies on building better businesses that are positioned to prosper over the longer term. The Sustainability improvements that we promote and encourage among our businesses benefit from our long-term view, and are underpinned by our focus on conducting business with the highest standards of integrity, honesty, and transparency.

By implementing a stronger culture of operational and financial improvement, we rebuild our businesses' resources and capabilities, and enable them to pursue commercially attuned Sustainability improvement initiatives.

2020 — A year in review

Justin Dowley
Chairman

Calendar year 2020

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

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

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

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

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

COVID-19 response

We and our businesses implemented strong and responsive measures during 2020 to mitigate the impact of COVID-19, primarily centred around enhanced cash management, minimising operational disruption, and above all else, protecting the health and safety of the Group's workforce. For further details, please refer to the Governance overview on pages 88 to 91.

Governance overview
Page 88

Dividend

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

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

Pensions

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

Board matters

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

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

Outlook 2021

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

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

J Dowley

Justin Dowley
Chairman
4 March 2021

Purpose, strategy and sustainability

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

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

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

- GKN Aerospace's H2Gear initiative to develop a ground-breaking UK hydrogen propulsion system to power a zero emissions aircraft;
- GKN Automotive's P4 eDrive powertrains, which reduce CO_2 emissions by up to 100%; and
- Nortek Air Management's StatePoint Technology®, which enables savings of up to 30% for energy consumption and up to 90% for water usage in giant data centre cooling systems around the world.

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

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

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

Sustainability report
Page 58

Simon Peckham
Chief Executive

Ensuring our businesses are fit for the future

"We buy high quality underperforming manufacturing businesses and invest in making them stronger, better businesses for the benefit of all stakeholders, whilst delivering good returns for shareholders."

We entered one of the most challenging years in Melrose's history with good momentum as our investments in operational improvements in the GKN businesses since acquisition began to take hold.

Results in the first quarter showed all businesses making good progress. However, the speed and scale of the onset of the COVID-19 pandemic in March forced a quick and strong adjustment in approach for the entire Group.

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

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

The impact of these decisions is clear from these results. Profit did decline significantly, albeit ending ahead of expectations at the height of the pandemic. The performance on cash generation has been exceptional. Our businesses have responded to the challenge laudably, generating £628 million in gross cash across the period. We are extremely grateful for the hard work from all our employees to produce this performance.

Performance in the second half, if annualised, was consistent with proforma debt leverage of approximately 3.2x EBITDA. This demonstrates the performance of our businesses this year and gives a sense of their capabilities as markets return.

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

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

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

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

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

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

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

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

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

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

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

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

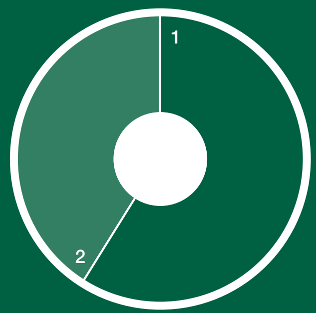
Simon A Peckham

Simon Peckham
Chief Executive
4 March 2021

Melrose Industries PLC Annual Report 2020

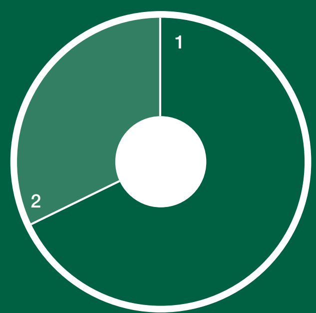
Aerospace

Revenue by market



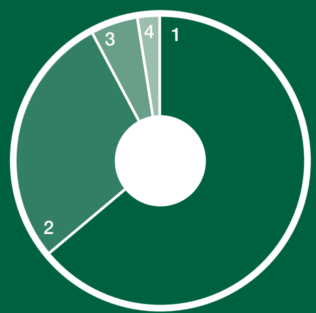
1 Civil	59%
2 Defence	41%

Revenue by market type



1 Airframes	68%
2 Engines	32%

Revenue by destination



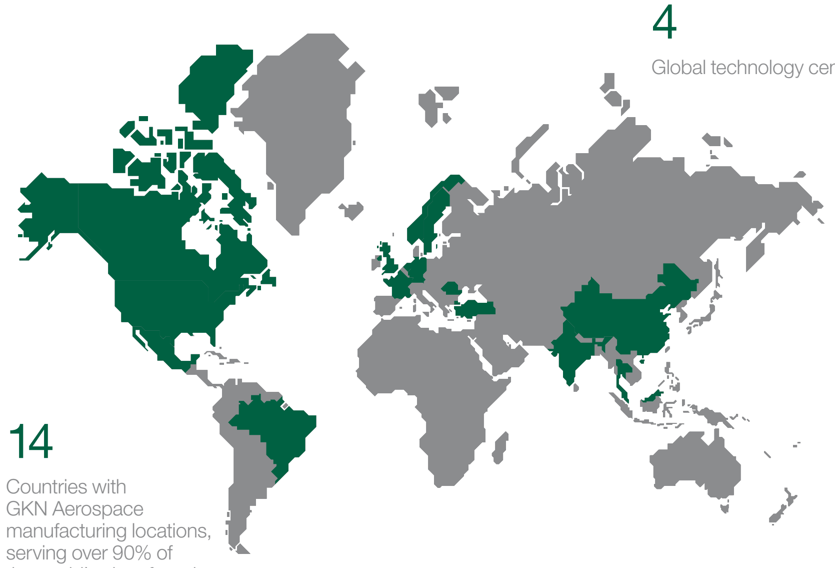
1 North America	66%
2 Europe	29%
3 Asia	4%
4 Rest of the world	1%

(1) All growth metrics are calculated at constant currency.

GKN Aerospace

GKN Aerospace is a world-leading multi-technology manufacturer of airframe and engine structures and electrical interconnection systems for the global aerospace industry, across both civil and defence platforms.

Operational geographies



4

Global technology centres

14

Countries with GKN Aerospace manufacturing locations, serving over 90% of the world's aircraft and engine manufacturers

Highlight figures

£2.8bn

Adjusted[1] revenue

£14m

Adjusted[1] operating profit

£2.8bn

Statutory revenue

£410m

Statutory operating loss

(1) Described in the glossary to the financial statements on pages 204 to 207.

(2) Based on adjusted[1] 2020 operating profit for all continuing trading businesses.

Proportion of Melrose[2]

30%

GKN AEROSPACE

GKN Aerospace is a global tier 1 aerospace business with market-leading positions driven by technological innovation, advanced processes and engineering excellence that help aircrafts fly safely, faster, further, and more sustainably.

Following a reorganisation in 2019, GKN Aerospace is structured according to its three core customer markets – Civil Airframe, Defence and Engines. It operates in 14 countries. GKN Aerospace's technology is used throughout the aerospace industry: from high-use single aisle aircraft and the world's longest haul passenger planes, through to business jets, helicopters, the world's most advanced fighter jets and space launchers.

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

gknaerospace.com

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

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

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

Civil Airframe continued its development of the Wing of Tomorrow with the National Composites Centre and initiated a new collaboration with Eviation to design and manufacture the wings, aircraft tail and electrical wiring systems for Alice, a ground-breaking regional electric aircraft.

(1) All growth metrics are calculated at constant currency.

Sustainability case study

The Fan Case Mount Ring that helps save fuel and waste

GKN Aerospace's continued innovation in Additive Manufacturing has enabled its development of a leading Fan Case Mount Ring (FCMR) structural design. GKN Aerospace's fan blade housing structure allows significant reduction in source material use, energy consumption and product weight, with a view to reducing greenhouse gas emissions in both the manufacturing process and across the product life cycle.

Technological advancements were made in 2020 using unique Laser Metal Deposition (LMD-w) fabrication techniques, enabling GKN Aerospace to secure its position as supplier of choice to Pratt & Whitney for the PW1500G engine, which will be used on the Airbus A220. The project is currently in its production start-up phase with first serial production expected in 2021.

GKN Aerospace's new fabricated FMCR promotes resource efficiency by reducing the buy-to-fly ratio from 15 in the original design to five. This represents a 60% reduction in material waste, which will save over 90 tonnes of forged titanium annually. Additionally, the FCMR reduces fuel burn by 20%, which translates to an estimated saving exceeding three million tonnes of CO_2 on products manufactured to date.

This project illustrates how GKN Aerospace is using its unique fabrication capability to reduce costs to its customers, and provide broader societal benefits by accelerating the reduction of aircraft fuel consumption.

Sustainability report
Page 58

In Engines, GKN Aerospace's world-leading additive manufacturing capability has led to the introduction of lighter and more efficient fan case mount rings, leading to a reduction of 20% in emissions and additionally has accelerated the inaugural flight testing of lightweight, recycled thermoplastic components with Bell on the V-280 Valor helicopter. It has commenced development of H2Gear, an exciting new hydrogen propulsion system for a zero emissions aircraft. In 2021, GKN Aerospace will also commence full operations at its flagship £32 million Global Technology Centre in Filton, UK, to work in partnership with the business's existing Global Technology Centres in the USA, Sweden and The Netherlands.

Throughout the year, GKN Aerospace further cemented its strategic position in the important Asia market that is benefiting from a relatively faster recovery after the initial wave of the COVID-19 pandemic.

In addition to the establishment of two wholly-owned production sites, one for windows in China and the other for engine components in Malaysia, GKN Aerospace also entered into a new strategic joint venture with a COMAC subsidiary to manufacture advanced aerostructures in Jingjiang, Jiansu Province, China. The state-of-the-art 80,000m^2 facility in Jingjiang will be GKN Aerospace's first aerostructures joint venture in China, and offers the opportunity to become an important part of local supply of advanced aerostructures in the region.

£54m

Collaborative H2Gear programme, to develop the technology required to accelerate the decarbonisation of the aerospace industry towards achieving net zero greenhouse gas emissions

Outlook

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

Market trends

Aerospace

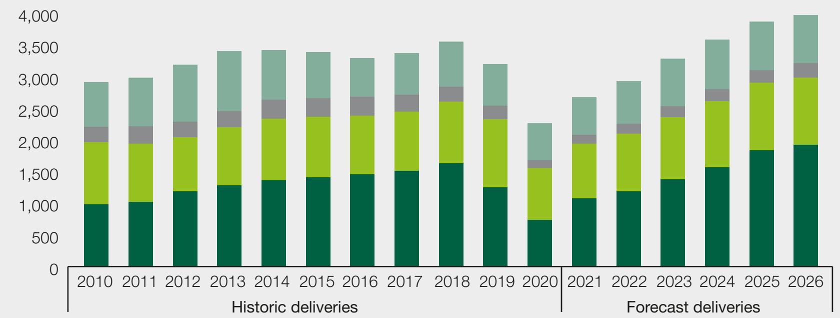
- The Civil aerospace market was severely impacted by the COVID-19 pandemic during 2020, with flight hours and aircraft deliveries substantially down for the year, and reduced future order books as airline customers faced liquidity challenges. The recovery is not expected to be swift.
- The Defence engines market was generally strong during 2020, principally driven by the US and European defence markets. The outlook remains healthy with international defence spending expected to remain stable for the coming years, offering significant opportunity for growth, with the exploration of potential future air combat programmes.
- The aerospace industry continued its significant drive towards more sustainable aviation, led by customers and governments.

GKN Aerospace has responded to these trends, by:

- Implementing cash management measures and reducing its cost structure to rationalise production swiftly and to significantly offset the impact of COVID-19.
- Maintaining and strengthening its position on key Defence platforms, including the F-35 and Gripen, and securing further positions for the business as a long-term contributor to the next generation of Defence platforms, including a position on Team Tempest in collaboration with BAE Systems and the UK Ministry of Defence.
- Setting a target of net zero greenhouse gas emissions by 2050 and taking significant steps to help decarbonise air travel by ensuring positions on key programmes to enable a sustainable long-term transformation of commercial aerospace, including projects to accelerate development and innovation for small electric, hydrogen propulsion, and sustainable aviation fuels.

Commercial aircraft deliveries by OEM[(1)]

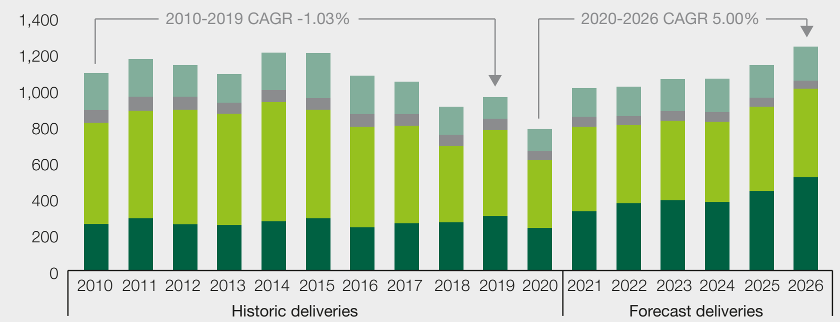
Civil aircraft | Business aircraft | Regional aircraft | Commercial rotorcraft



(1) Source: Fleet Discovery, Aviation Week Network, Copyright 2020.

Military aircraft production in number of deliveries[(2)]

Fighters | Rotorcraft | Military transports | Trainers/Light attack



(2) Source: Source: Fleet Discovery, Aviation Week Network, Copyright 2020.

Melrose Industries PLC Annual Report 2020

Automotive

GKN Automotive

GKN Automotive is a leading supplier of driveline technologies to the global automotive industry and a trusted partner to over 90% of the world's car manufacturers for electrification, all-wheel drive programmes and new vehicle concepts.

Proportion of Melrose[2]

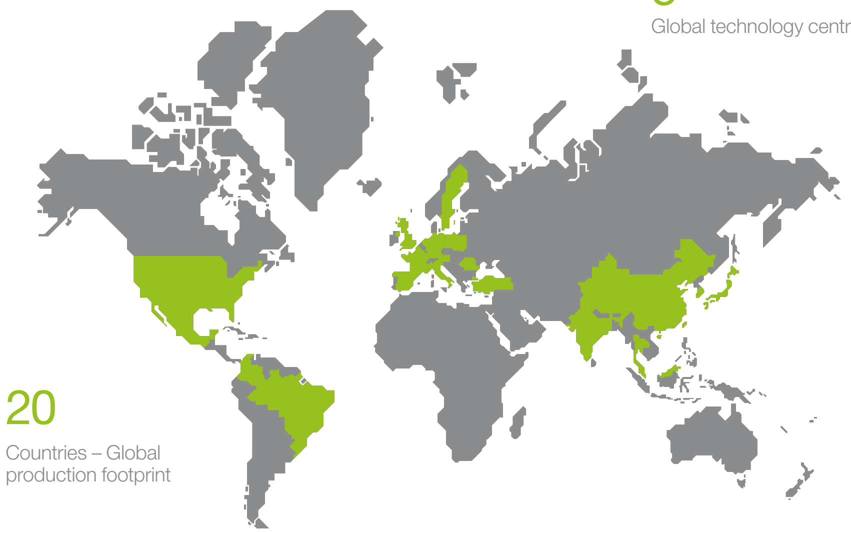
41%

GKN AUTOMOTIVE

GKN Automotive is a global leader in drive systems for all segments of the automotive industry, from the smallest ultra-low-cost cars to the most sophisticated premium vehicles demanding the most complex driving dynamics, almost 50% of cars sold worldwide use GKN Automotive technologies.

GKN Automotive has operations in 20 countries and is primarily organised around two major business divisions: (i) Driveline, the global leader in driveline technologies with an extensive portfolio of products covering sideshafts, propshafts and constant velocity joints for every type of propulsion system whether that be hybrid, electric or internal combustion; and (ii) ePowertrain, a global leader and pioneer with over 18 years' experience in electric drive technologies ("eDrive") and intelligent all-wheel drive ("AWD") systems.

Operational geographies



5
Global technology centres

20
Countries – Global production footprint

Highlight figures

£3.8bn
Adjusted[1] revenue

£82m
Adjusted[1] operating profit

£3.2bn
Statutory revenue

£183m
Statutory operating loss

(1) Described in the glossary to the financial statements on pages 204 to 207.

(2) Based on adjusted[1] 2020 operating profit for all continuing trading businesses.

(1) All growth metrics are calculated at constant currency.

gknautomotive.com

Revenue by product type

1	Driveline	71%
2	All-wheel drive	25%
3	eDrive	3%
4	Cylinder Liners	1%

Revenue by destination

1	Europe	35%
2	North America	33%
3	Asia	28%
3	Rest of the world	4%

Divisional review(1)

Continued

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

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

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

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

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

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

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

Outlook

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

Sustainability case study

Battery Electric Vehicle P4 eDrive System reduces carbon emissions from vehicles

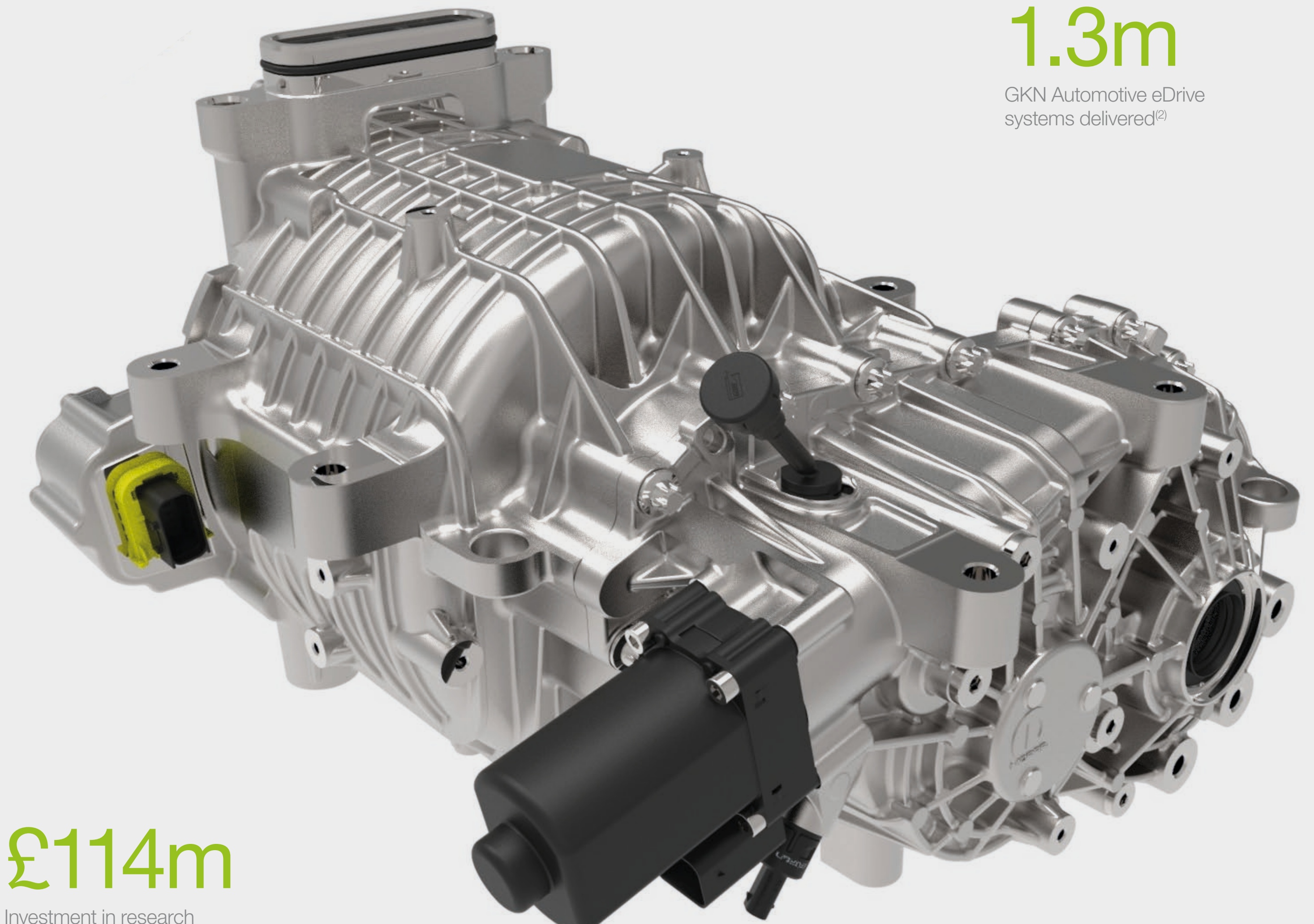
GKN Automotive has long been committed to the sustainable development and commercialisation of advanced eDrive technologies. The business's product stewardship provides tangible benefits for the environment, with annual savings of around 180,000 tonnes of CO_2 generated by eDrive products sold in 2020 alone.

In 2020, GKN Automotive launched its 2-in-1 (gearbox and eMotor) P4 eDrive system for use in a major zero-emissions small city battery electric vehicle (BEV). The design applied key technological components which have been integral to the evolution of the eDrive systems including the 210H eMotor, the offset gearbox design with integrated eMotor active parts, and application of the standard park lock.

GKN Automotive's technology is helping vehicle manufacturers to lower the average CO_2 emissions of their fleet. In one example, an all-electric variant of a high-volume hybrid produces 0 grams of CO_2 per kilometre in use, versus 119 grams of CO_2 per kilometre in use for the hybrid model.

GKN Automotive aims to bring advanced, compact and efficient electric drive systems to more vehicles, allowing more customers to reduce their climate impact.

Sustainability Report
Page 58



1.3m

GKN Automotive eDrive systems delivered(2)

£114m

Investment in research and development

(1) All growth metrics are calculated at constant currency.
(2) Up to 31 December 2020.

Market trends

Automotive

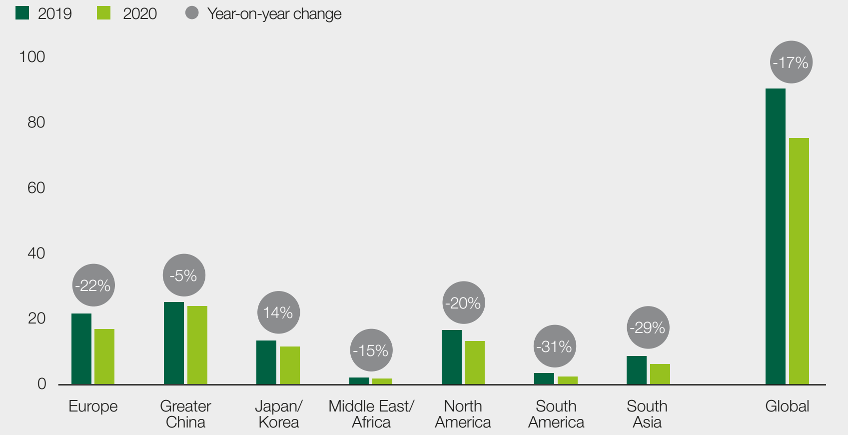
The global COVID-19 pandemic resulted in strong headwinds and volatility in the automotive sector in 2020, the most significant of which being:

- Volume decline: global light vehicle production was down 17% year-on-year 2020 vs. 2019, driven by Europe (-22%) and North America (-20%).
- Recovery rate variability: light vehicle production recovery rates are expected to vary across regions, as depleted levels of inventory need to be replenished in parallel to the re-establishment of a baseline for local consumer demand. 2021 vs. 2020 production rates are projected to be +15% in Europe, +25% in North America and +6% in China and +14% on a global level.
- Acceleration in eDrive development: the incentives attached to COVID-19 governmental recovery packages, along with broader legislative tightening, have accelerated the adoption of electrification and new mobility solutions. Global electric vehicle penetration is projected to increase, with BEV/PHEV share of production in 2027 now forecasted to be 29% (versus a projection of 24% this time a year ago).
- Macro-economic uncertainty: as a result of the impact of new trading policies (particularly the US), uncertainty around trade tariffs (particularly between the US and China) and legislative changes associated with Brexit and other factors.

GKN Automotive responded to the COVID-19 pandemic by strengthening its supply chain, investing in eDrive technology, and maintaining close relationships with customers and suppliers. These measures will allow the business to respond in a dynamic manner to the rebound.

Market dynamics COVID impact felt across all regions

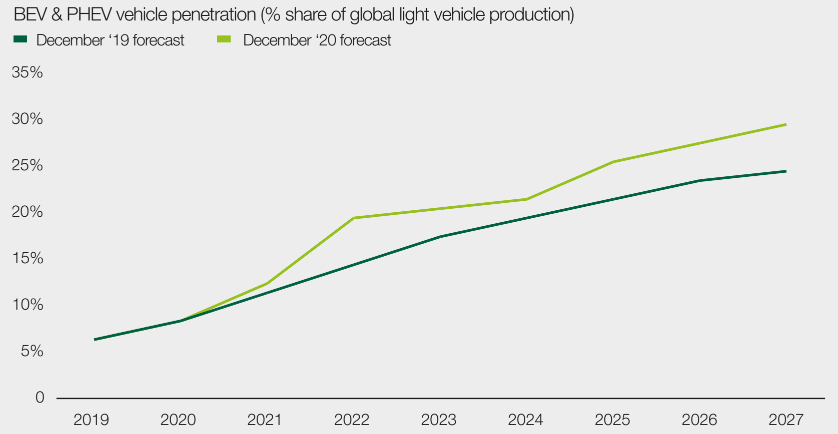
Figure 1: Change in light vehicle production per region (2019 v 2020, million vehicles)(1)



(1) Source: IHS light vehicle production, December 2020.

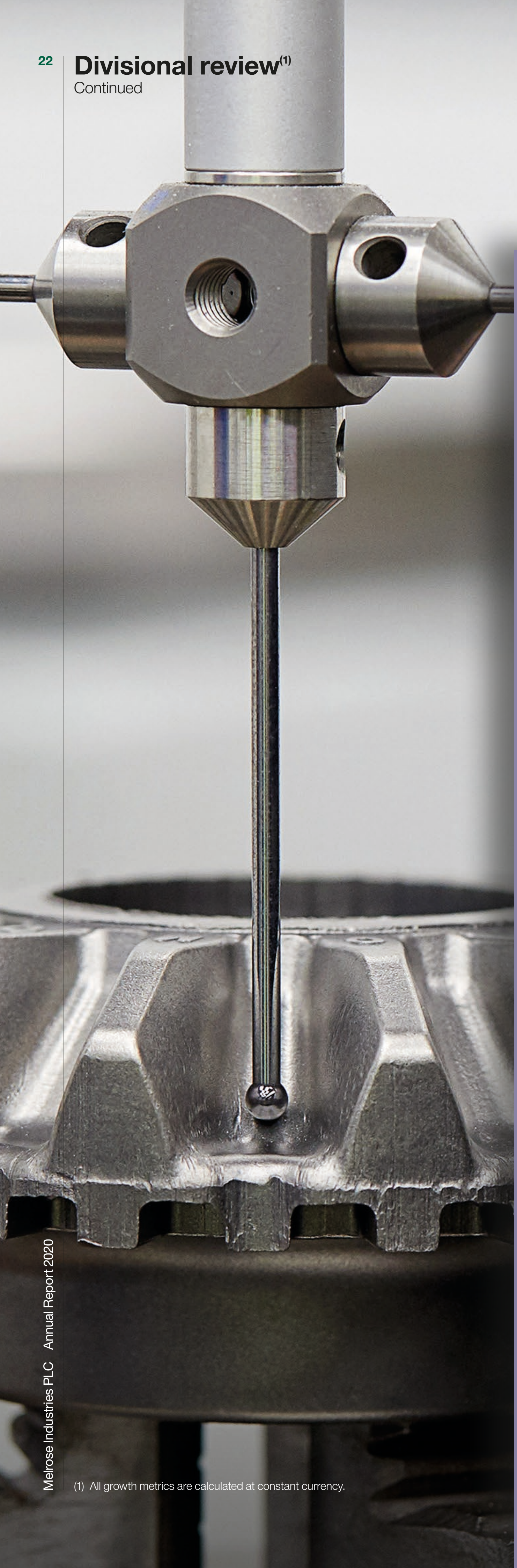
Market dynamics BEV penetration

Figure 2: Change in electric vehicle penetration (Dec 2019 vs. Dec 2020)(2)



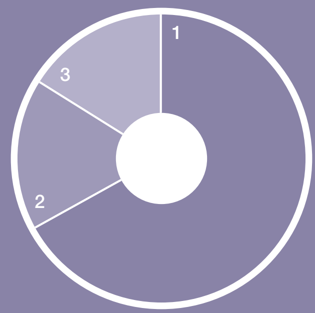
(2) Source: IHS light vehicle production, December 2020.

Melrose Industries PLC Annual Report 2020



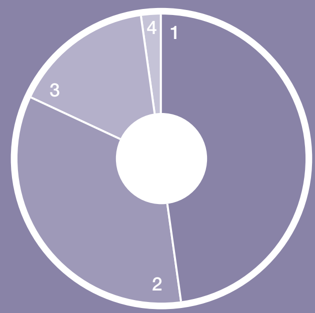
Powder Metallurgy

Revenue by market type



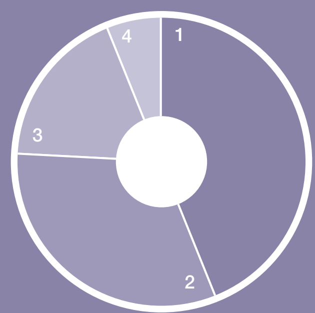
1	Automotive	67%
2	Industrial	17%
3	Hoeganaes Metal Powder	16%

Revenue by segment



1	Precision	48%
2	Structural	34%
3	Powder	16%
4	Additive	2%

Revenue by destination



1	North America	44%
2	Europe	32%
3	Asia	18%
4	Rest of the world	6%

(1) All growth metrics are calculated at constant currency.

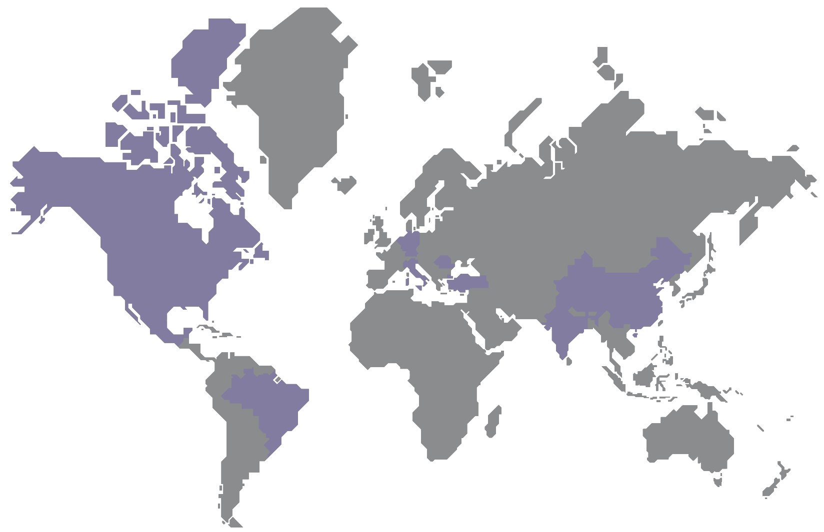
Powder Metallurgy

GKN Powder Metallurgy is a global leader in both precision powder metal parts for the automotive and industrial sectors, and the production of metal powder, through its prized vertically integrated business platform.

Proportion of Melrose(2)

10%

Operational geographies



Global Technology Centres
Germany, Italy, US

Highlight figures

£905m
Adjusted(1) revenue

£39m
Adjusted(1) operating profit

£886m
Statutory revenue

£57m
Statutory operating loss

(1) Described in the glossary to the financial statements on pages 204 to 207.
(2) Based on adjusted(1) 2020 operating profit for all continuing trading businesses.

GKN POWDER METALLURGY

GKN Powder Metallurgy combines advanced powder metals with innovative production technologies to create unique metal products – smart, reliable and precise.

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

gknpm.com

Divisional review(1)

Continued

Sustainability case study

Hy2green helps you live and work 'off-grid'

Hydrogen is set to become one of the most versatile zero emissions fuels of the future.

GKN Powder Metallurgy's Hy2green storage system is ideal to produce and store hydrogen locally from carbon-free renewable energy sources.

'Green' hydrogen is made by extracting hydrogen from water using electrolysis powered by renewable energy. Hydrogen is a zero-emissions fuel, producing just water and oxygen as waste products. GKN Powder Metallurgy's Hy2green solution enables hydrogen to be stored safely in low pressure metal hydrides, before being used directly in electric power and heat generation, and mobility solutions, helping customers towards achieving energy self-sufficiency. This technology reduces the physical space required to store the same volume of hydrogen compared to gaseous hydrogen storage, allowing it to be stored easily for as long as needed.

GKN Powder Metallurgy's Hy2green technology benefits from 100% recyclability of the metal powder used in its metal hydride component, whilst offering a robust energy supply that maintains 100% capacity after three years of use. This capability for long-term storage enables seasonal energy buffering, whereby energy generated in summer months can be used as heat and electricity in the winter.

GKN Powder Metallurgy offers its Hy2green technology in a range of energy storage capacities, allowing for numerous applications including back-up power, charging, residential and maritime. Hy2green products will allow customers to better utilise clean energy, helping them achieve their net zero goals and reduce their climate impact. Validation projects through 2020 have shown the system to be safe, robust, and scalable, and the system is expected to be officially launched to market in 2021.

Sustainability report
Page 58

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

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

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

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

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

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

Outlook

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

Market trends

Powder Metallurgy

2020 was a year of substantial and accelerated change in GKN Powder Metallurgy's major markets. The push towards digital and electrification gained momentum. As a leader across all of its markets, GKN Powder Metallurgy remains well placed to gain short and medium-term advantages. The major trends in its core automotive and industrial markets are primarily being driven by the following factors:

- Customers reducing their supplier base and staying with the technology leaders that can serve their global requirements.
- Customers demanding increased manufacturing efficiency, functionality and flexibility through digitisation.
- Legislative clamp-downs to reduce emissions.
- The increase of electrified vehicles and manufacturing equipment.
- Readiness of adaption of the current business model to take advantage of the digital/virtual opportunities.

These trends are driving greater digitalisation in all markets in which GKN Powder Metallurgy operates. There remains significant growth potential in the additive manufacturing markets for both materials and components. The benefits of GKN Powder Metallurgy's acquisition of FORECAST 3D, which completed in January 2020, are expected to accelerate primarily through increased market penetration in 2021, and by opening two new printing hubs in Auburn Hills, US and Bonn, Germany.

(1) All growth metrics are calculated at constant currency.

Nortek Air Management

Nortek Air Management

The Nortek Air Management division comprises (i) Nortek Global HVAC ("HVAC") and (ii) Air Quality and Home Solutions ("AQH").

Proportion of Melrose(2)

13%

Operational geographies

Highlight figures

£1.2bn
Adjusted(1) revenue

£188m
Adjusted(1) operating profit

£1.2bn
Statutory revenue

£149m
Statutory operating profit

(1) Described in the glossary to the financial statements on pages 204 to 207.
(2) Based on adjusted(1) 2020 operating profit for all continuing trading businesses.

(1) All growth metrics are calculated at constant currency.

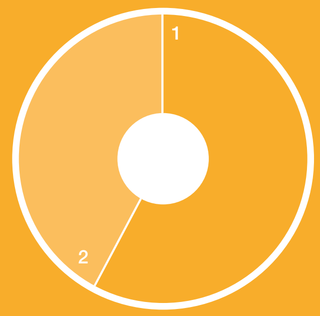
The HVAC business includes the custom and commercial business of Nortek Air Solutions, the residential and light commercial business of HVAC and the dedicated data centre business of StatePoint Liquid Cooling. It employs a strategic framework of sustained profitable growth, operational excellence, technological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

nortekhvac.com
nortekair.com

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

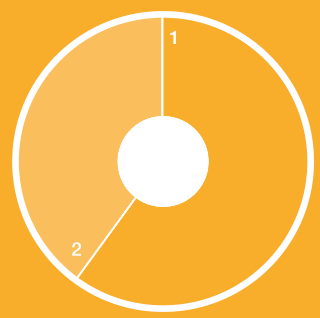
broan-nutone.com

Revenue by business



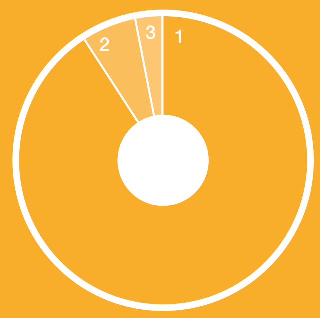
1	Nortek Global HVAC	58%
2	Air Quality and Home Solutions	42%

Revenue by market



1	Residential	60%
2	Commercial	40%

Revenue by destination



1	North America	91%
2	Europe	6%
3	Asia	3%

Melrose Industries PLC Annual Report 2020

Nortek Global HVAC

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

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

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

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

Outlook

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

Market trends
Nortek Global HVAC

- The global data centre market is expected to grow at over 13% CAGR through to 2025. North America represents c.35% of the data centre market and is expected to grow at 11% CAGR.
- Sustainability has become an important initiative for data centre operators. Energy, water and space utilisation have become critical to reduce cost to ensure regulatory compliance and to satisfy strong demand for carbon footprint reduction.
- Construction spending for North America is forecasted to be flat in residential and negative across many of NAS commercial/institutional sectors through to 2023. Retrofit and refurbishment are expected to see modest growth for commercial and residential, respectively.
- Within the non-residential construction sector, put-in-place construction was previously forecasted to grow, but is now forecasted to decline in the US and Canada due to the impact of COVID-19.
- Commercial office and education building projects were hardest hit during 2020 as companies assessed the acceleration of the shift to flexible working arrangements. In higher education, new construction spending is expected to reduce and a shift in focus towards ensuring strong maintenance, wellness, and health and safety within existing buildings.

HVAC shall continue to serve its core markets through technological innovation and product leadership, to provide infrastructural solutions that seek to overcome continued environmental and regulatory pressures aimed at reducing energy and water usage intensity, and reducing carbon emissions, to enable consumers and businesses to act in a more sustainable manner.

Sustainability case study

StatePoint substantially reduces energy and water usage in global data centres

Nortek Global HVAC's StatePoint Technology® is the world's first sustainable data centre cooling system, and is designed to substantially reduce water and power usage in hyperscale data centres. The cutting-edge design reduces power usage by 30% compared with conventional designs and reduces water consumption by up to 90% in cooler climates. These environmental benefits help to avoid over-burdening local water supplies and eliminate the need for refrigerant-based cooling that can have a significant global warming impact.

The flexible StatePoint design can be used in any data centre regardless of location or climate, and maintains sustainable, efficient performance. The hyperscale data centre market has a compound annual growth rate of 19%, meaning that power and water usage associated with cooling such facilities will increase at a similar rate. StatePoint offers an environmentally responsible solution to this growth, minimising water and energy usage and significantly reducing emissions.

Sustainability report
Page 58

Air Quality and Home Solutions

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

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

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

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

Outlook

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

Market trends
Air Quality and Home Solutions

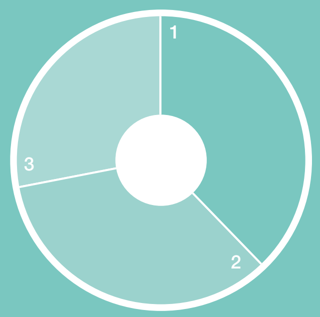
- Outlook for the home improvement industry remains positive, driven by the stay-at-home impact of COVID-19. However, the timing and rate of recovery remains uncertain.
- Digital shopping and online purchasing is expected to continue, with growth in these sales channels expected to be driven by longer-term trends away from traditional physical sales channels.
- Rising home prices and traditionally lower interest rates should continue to encourage homeowners to engage in ongoing maintenance and repair spending.
- The COVID-19 pandemic is expected to continue to highlight ventilation and fresh air solutions for homes and buildings.

AQH continues to bring new, refreshed and innovative products to market across multiple categories that address market demands and competitive pressures. Meeting customer needs for 'whole house' ventilation solutions will continue to be a focus for the business in 2021, with the demand for connectivity expected to continue to grow significantly over the longer-term, with increasing demand from the most sustainability-conscious house builders.

(1) All growth metrics are calculated at constant currency.

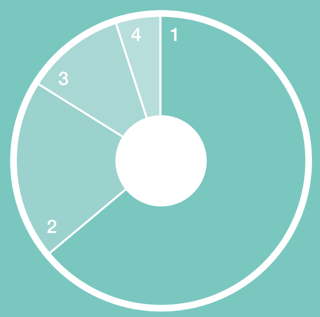
Other Industrial

Revenue by business



1	Nortek Control	38%
2	Ergotron	34%
3	Brush	28%

Revenue by destination



1	North America	64%
2	Europe	20%
3	Asia	11%
4	Rest of the world	5%

(1) All growth metrics are calculated at constant currency.

Other Industrial

The Other Industrial division comprises (i) Brush, (ii) Nortek Control, and (iii) Ergotron.

Operational geographies

Highlight figures

£628m
Adjusted[1] revenue

£63m
Adjusted[1] operating profit

£628m
Statutory revenue

£34m
Statutory operating profit

(1) Described in the glossary to the financial statements on pages 204 to 207.
(2) Based on adjusted[1] 2020 operating profit for all continuing trading businesses.

Proportion of Melrose[2]

6%

BRUSH

Brush is a leading independent provider of Turbogenerators, Transformers and Switchgear, and a provider of Services across these core product segments.

brush.eu

NORTEK CONTROL

Nortek Control is a leading developer and manufacturer of security, home automation, access control, health and artificial intelligence technologies for the residential and commercial markets, principally in North America.

nortekcontrol.com

ergotron

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

ergotron.com

Divisional review[1]
Continued

Brush

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

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

Outlook

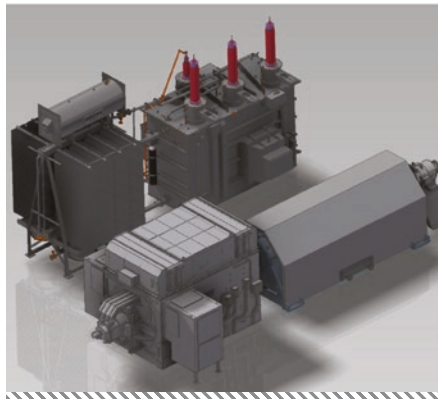
Brush is now a profitable, cash-generative business. Having demonstrated that it is more agile than ever before, it has secured a positive order backlog stretching well into 2021 and beyond, and firm foundations for improvement based upon a more diversified customer portfolio across a broad range of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

Market trends
Brush

- Renewable electricity generation is projected to grow by almost 7% in 2021, with wind and solar PV expected to continue to set new records in 2021[1].
- With a recovery of the global economy in 2021, global electricity demand is expected to grow by around 3%, largely driven by emerging and developing economies, particularly China and India[2].
- Brush continues to target market opportunities in helping network operators address the challenge of supply volatility associated with increased renewables within the grid, delivering increased asset performance visibility, and the digitalisation of service monitoring.

(1) Source: Renewable electricity net capacity additions by technology, main and accelerated cases, 2013-2022 – Charts – Data & Statistics – IEA.
(2) Source: Electricity Market Report December 2020 – IEA.

(1) All growth metrics are calculated at constant currency.



Sustainability case study

Brush – Synchronous Condenser helps unlock renewable power generation

Brush's Synchronous Condenser is helping to address the global problem of electrical distribution network instability caused by renewable power generation and transmission.

The global drive for renewable energy has added significant solar and wind-generated power to the grid. Renewable power is primarily generated via static systems which, when generating and transmitting power from renewable sources in larger volumes, cause grid instability in respect of voltage, frequency, and power factor fluctuations, which can result in significant challenges to overall network stability.

Brush's Synchronous Condensers overcome such challenges and enhance grid stability by providing greater inertia, reaction power compensation, and short circuit power capacity. This offers significant cost savings by removing the need to invest in infrastructure reinforcements, such as new transmission lines, that would otherwise be required to address the issue. Brush's Synchronous Condensers bring differentiation to its Generator portfolio, providing strong value positioning to customers and creative solutions to the challenges posed by renewable power expansion.

Sustainability report
Page 58

Nortek Control (formerly Security & Smart Technology)

Nortek Control continues to bolster its expertise in the design and manufacture of analytics-embedded wireless connectivity devices, to leverage its strong brand presence in professional security, integrator and custom installer channels.

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

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

Outlook

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

Market trends
Nortek Control

The Nortek Control business operates in a residential security and home automation market that continues to be driven by connected solutions that interact and integrate within the ever-expanding Internet of Things product space to provide enhanced functionality, and continues to be challenged by lockdown restrictions, which prevent installers from physically accessing their customers. Nortek Control continues to invest and bring to market new products with enhanced features and improved connectivity, including the new EDGE panel from 2GIG which will be the most advanced residential security system in the industry, Linear's new garage operator product line, which is compatible with large online retailers allowing drivers to secure packages inside a customer's garage, and the launch of Numera's tele-medicine portal, VitalStream, which will allow patients to send daily diagnostics to healthcare providers directly from their homes.

Ergotron

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

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

Outlook

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

Market trends
Ergotron

The Healthcare market continues to present significant expansion opportunity driven by an increased focus on improving patient interaction. New growth opportunities within the Office market are expected from the emerging longer-term shift to hybrid working models. The Education segment continues to transition towards hybrid and distance learning models, fuelled by the digitalisation of education and the renewed focus on home learning solutions. The Industrial segment continues to target increased shop floor digitalisation.

Ergotron is already responding to these market trends through its broad product offering, most notably in Healthcare from industry-leading mobile carts to wall-mounted solutions that can be integrated with specific applications, including TeleHealth technology. The ongoing emphasis on home office working, and the expected revival of Ergotron's Industrial workflow and ergonomic solutions including mobile stations and industrial arms, are set to propel the business's growth in these segments in 2021.

Sustainability case study

Ergotron – bespoke Vaccination Carts deliver COVID-19 vaccines to the public

The unprecedented challenges posed by the COVID-19 pandemic have heightened the need for accessible, quality healthcare solutions, and Ergotron's professional-grade medical carts directly addressed this critical need during 2020. By implementing rapid measures including the redeployment of resources to medical cart production as and when required, and responsive supply chain optimisation, Ergotron adapted its operations throughout 2020 to ensure that their medical carts could reach customers faster.

Ergotron's medical cart design was modified in response to the global vaccine rollout, to cater for mobile COVID-19 vaccination distribution to suit mass vaccination sites that were set up in non-traditional spaces, such as car parks and stadiums. The cart also supports Ergotron's patented LiFeKinnex™ Technology for reliable battery power without an outlet, overcoming limitations imposed by power availability outside of optimised healthcare settings. Ergotron's flexible carts are facilitating the expansion of vaccination workflows beyond the walls of traditional clinical environments, providing convenient access to critical supplies for caregivers.

Sustainability report
Page 58

Measuring our performance

In order to support the Group's strategy and to monitor performance, the Board uses a number of financial and non-financial key performance indicators ("KPIs").

The immediate and significant impact of the COVID-19 pandemic on the Group resulted in a decision to prioritise cash generation in the year ended 31 December 2020. As a result, additional KPIs are presented below.

Additional business-level KPIs are also used, which are relevant to their particular circumstances. Further detail on these KPIs is disclosed in the glossary to the financial statements and further information regarding the performance of the Group against its financial KPIs is included in the Finance Director's review.

Financial KPIs

Financial KPIs	Method of calculation	Strategic objective
Adjusted[(1)] diluted earnings per share 2.4p '18 12.7p '19 14.3p '20 2.4p	Group adjusted[(1)] profit after tax of continuing businesses, attributable to owners of the parent, for the year ended 31 December 2020, divided by the weighted average number of diluted ordinary shares in issue.	To create consistent and long-term value for shareholders.
Adjusted free cash generation[(1)] £628m '18 £343m '19 £591m '20 £628m	Total cash generated from continuing operations after all costs, excluding restructuring, one-off payments to defined benefit pension schemes and net transaction related costs or income.	To ensure subsidiary businesses are suitably cash-generative in order to have adequate cash reserves for the effective running of the Group and for significant capital investment where required.
Net debt[(1)] reduction 13% '18 N/A[(2)] '19 8% '20 13%	Reduction in net debt in the year as a percentage of opening net debt.	To ensure that the Group has suitable amounts of net debt and remains within its banking covenants.
Adjusted[(1)] profit conversion (pre-capex) to cash percentage 167% '18 90% '19 104% '20 167%	Percentage of adjusted[(1)] EBITDA[(3)] conversion to cash, as shown in the glossary to the financial statements, for continuing businesses in existence during the year ended 31 December 2020 pre-capital expenditure.	To ensure subsidiary businesses are suitably cash-generative in order to have adequate cash reserves for the effective running of the Group and for significant capital investment where required.
Adjusted[(1)] operating profit £340m '18 £813m '19 £1,102m '20 £340m	Adjusted[(1)] operating profit for the continuing businesses in existence during the year ended 31 December 2020.	To improve profitability of Group operations.
Net debt to adjusted[(1)] EBITDA[(2)] 4.1x '18 2.28x '19 2.25x '20 4.1x **Net debt to H2 annualised proforma adjusted[(1)] EBITDA[(2)]** 3.2x	Net debt to adjusted[(1)] EBITDA[(2)] – net debt at average exchange rates divided by adjusted[(1)] EBITDA[(2)] further adjusted to reflect covenant requirements, for continuing businesses at each year end. Net debt to H2 annualised proforma adjusted[(1)] EBITDA[(2)] – net debt at H2 average exchange rates divided by H2 annualised adjusted[(1)] EBITDA[(2)] further adjusted to reflect covenant requirements, for continuing businesses.	To ensure the Group has suitable amounts of debt and remains within its banking covenants following the re-basing of the leverage and interest cover covenants as a result of the impact of the COVID-19 pandemic.
Adjusted[(1)] operating profit margin 3.6% '18 9.4% '19 9.5% '20 3.6%	Adjusted[(1)] operating profit as a percentage of adjusted[(1)] revenue, for the continuing businesses in existence during the year ended 31 December 2020.	To improve profitability of Group operations.
Interest cover 5.1x '18 11.6x '19 10.8x '20 5.1x	Adjusted[(1)] EBITDA[(2)] further adjusted to reflect covenant requirements of all businesses as a multiple of net interest payable on bank loans and overdrafts for the Group during each year.	To ensure the Group has sufficient profitability to meet the interest cost of debt and remains within its banking covenants following the re-basing of the leverage and interest cover covenants as a result of the impact of the COVID-19 pandemic.
Final dividend per share[(4)] 0.75p '18 3.05p '19 0.00p '20 0.75p	Amount declared as payable by way of dividends in terms of pence per share.	To operate a progressive dividend policy whenever the financial position of the Company, in the opinion of the Board, justifies the payment. For discussions on the dividend, please refer to the Chairman's statement on pages 10 to 11.

(1) Described in the glossary to the financial statements on pages 204 to 207.
(2) Net debt increased during 2018 as a result of the acquisition of GKN.
(3) Operating profit before depreciation of property, plant and equipment and amortisation of computer software and development costs.
(4) The initially proposed final dividend for the year ended 31 December 2019 of 3.4 pence per ordinary share was withdrawn as announced on 7 May 2020 following the impact of the COVID-19 pandemic.

Non-financial KPIs

Health and safety

In line with the Melrose decentralised model, Group business units are responsible for implementing and maintaining health and safety excellence across their operations. To provide visibility and oversight for the Board, information is collated quarterly on three key performance indicators – Major Accident Frequency, Accident Frequency, and Accident Severity (as defined below) – for each business and covering all of their sites. A variety of additional health and safety KPIs are used by the businesses owned by the Group from time to time, which are specific to the exact nature of the business and its associated risks. Although responsibility for health and safety rests with the business units, in the unfortunate circumstance of a very serious incident, the Melrose senior management team will engage directly with the relevant business unit executive team and report any actions taken directly to the Board. There have been no such incidents during the period.

Method of calculation

In 2018, the Nortek and Brush businesses harmonised their KPI outputs and, following the acquisition of GKN, the KPI outputs for the GKN businesses were also migrated onto the Melrose reporting metrics. Given the expansion and diversified nature of the Group following the GKN acquisition, weightings have been applied to each division's reported health and safety performance according to the size of its workforce relative to that of the other divisions within the Group. Therefore, the larger the workforce, the more heavily such division's health and safety performance drives the Group-wide performance figures.

Strategic objective

The Company has an objective to stop all preventable accidents.

Performance[(1)]

The Group's current businesses measure three key health and safety KPIs:

Major accident frequency rate 0.19

'18 0.21
'19 0.50
'20 0.19

Records the average number of lost time accidents that have resulted in more than three days off work (defined as 'major' accidents), per 200,000 hours worked.

Accident frequency rate 0.30

'18 0.47
'19 0.43
'20 0.30

Records the number of all lost time accidents, both major and minor, per 200,000 hours worked.

Accident severity rate 20.39

'18 22.08
'19 18.97
'20 20.39

Records the average number of days an employee takes off work following an accident at work.

The Group's major accident frequency rate, accident frequency rate and accident severity rate decreased year-on-year for each business within the Group, except for GKN Aerospace's accident severity rate, which increased due to two specific incidents. The Group's trajectory of longer-term improvement continues, and our businesses continue to uphold and further develop high standards of health and safety performance. The general trend of improvement reflects that continued investment in health and safety initiatives across all businesses has taken hold, having achieved year-on-year sustained improvement, and highlights a distinct culture shift during Melrose's stewardship since the Nortek businesses were acquired in 2016, and strong trajectory of continual improvement in the GKN businesses since they were acquired in 2018.

At the Board's request, external health and safety experts are engaged through the Group's insurance brokers to review the health and safety audit function for each GKN business and verify its operation through one or more site visits. This review programme provides assurance of the robustness of the health and safety systems that operate within the Group's larger and most complex businesses. Recommendations are fed back to the relevant business unit executive team to manage their implementation as part of the usual continuous improvement efforts.

During 2020, the Group's insurance brokers in conjunction with the health and safety leads at each of the GKN businesses completed their initial review of their divisional health and safety audit functions and conducted verification site visits where possible in light of COVID-19 disruption. The reviews confirmed that business is operating to an acceptable standard, with a strong commitment to health and safety both centrally and at site level. In parallel with existing business unit-led initiatives, the Group's insurance brokers in the US conduct independent health and safety compliance audit reviews across the Group's US-based businesses, in close consultation with the businesses' HSE leads. This helpfully covers the Nortek businesses not included in the audit review process referred to above. US air and overnight travel restrictions delayed site visits for most of 2020. Plans are in place for site visits to recommence as early as practicable during 2021, as restrictions are anticipated to lift. The US audits assess for potential major and serious injuries and fatalities exposures such as machine guarding, manual material handling, forklift/powered industrial trucks, occupational health exposures including noise and chemical exposures, and confined spaces.

During 2020, each business in the Group took responsive action and implemented and maintained measures and protocols to address the risks of a COVID-19 outbreak within the workplace, and to support their employees in line with national guidelines. This included the use of relevant PPE, social distancing measures where practicable, protocols to support safe working practices including adjusted shift patterns, and tracing and identification measures to address instances of employees contracting the virus so as to protect the workforce, mitigate the risk of spreading, and minimise disruption to operations where possible. These measures continue to be monitored by the business unit executive teams to keep their employees safe. Further details are provided in the Sustainability report on pages 58 to 87.

Environment and energy usage

Method of calculation

Due to the decentralised nature of the Group and differing operations of businesses which the Company may acquire, there are no standardised environmental KPIs used throughout the Group. Businesses provide data for relevant environmental indicators, including energy consumption, CO_2 emissions, water consumption, waste disposal, solid waste generation, and recycling. We have used the UK Government Environmental Reporting Guidelines including the UK's Streamlined Energy and Carbon Reporting requirements and the GHG Protocol Corporate Accounting and Reporting Standard (revised edition), and data has been gathered in accordance with our GHG reporting procedure.

Strategic objective

Melrose fully understands the importance of the Group's environmental responsibilities and is committed to encouraging our businesses to make efficiency improvements where possible and to run their operations with a minimum possible adverse effect on the environment.

Performance

Information in relation to the various environmental initiatives undertaken by the Group's businesses during 2020 can be found within the Sustainability report on pages 58 to 87. The Group is required to disclose its greenhouse gas emissions and certain energy use data for the year ended 31 December 2020. Such data can be found within the Sustainability report on pages 58 to 87.

Other non-financial KPIs

Due to the diverse nature of the Group, each business acquired by the Group uses a range of its own specific non-financial KPIs, which are used to drive business performance and assist in managing risk. This helps to ensure that the KPIs used are relevant to each business and take into account specific operational and reporting requirements. Such KPIs cover operational, quality, commercial and human resource measures. Further information regarding some of the Group's recent initiatives in these areas can be found within the Sustainability report on pages 58 to 87.

(1) National lockdown measures and Government recommendations to stay at home in certain countries due to COVID-19 caused certain sites within the Group to experience lower employee attendance at limited times of the year during 2020.

Robust cash management was set as the top commercial priority for the Group this year.

As a result, an adjusted free cashflow of £628 million was generated in the year, 6% more than the adjusted free cash generated in 2019.

Geoffrey Martin
Group Finance Director

Melrose Group results – continuing operations

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

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

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

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

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

Statutory revenue **£8.8bn**

Adjusted revenue **£9.4bn**

Reconciliation of statutory results to adjusted results

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

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

Adjusting revenue item:

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

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

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

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

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

- A charge of £110 million (2019: £79 million) within the Aerospace division primarily relating to costs incurred globally to reduce the business' headcount and cost structure in reaction to the significant impact that COVID-19 is having on the aerospace industry. This charge also included costs in respect of the continuation of the business' global integration, announced last year, to create "One Aerospace", ensuring the business is well positioned and able to react to changes in its new environment; and the continuation of costs relating to rationalisation projects commenced in the previous year.
- A charge of £60 million (2019: £83 million) within the Automotive division as the business has accelerated its efforts to address its high cost base, inherited on acquisition, and best position itself as it recovers post COVID-19.
- A charge of £48 million (2019: £19 million) within the Powder Metallurgy division including costs associated with realigning the business for future demand, along with consolidation actions started in 2019 and the commencement during 2020 of the closure of a site in its underperforming North American Structural business.
- A net charge of £2 million (2019: £57 million) within the Nortek Air Management, Other Industrial and Corporate divisions which includes the completion of a factory consolidation within the HVAC business; the finalisation of the changes made in the Nortek Control business (formerly the Security & Smart Technology business) to move to a third party contract manufacturing model; and the profit from the disposal of a Dutch property held within the Brush business left vacant following the factory consolidation programme commenced in 2018.

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

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

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

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

Finance Director’s review
Continued

Statutory and adjusted results by reporting segment

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

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

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

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

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

Finance costs and income – continuing operations

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

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

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

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

Discontinued operations

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

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

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

Tax – continuing operations

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

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

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

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

Melrose employee share plan

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

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

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

Cash generation and management

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

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

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

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

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

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

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

The movement in net debt is summarised as follows:

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

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

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

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

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

Assets and liabilities

The summarised Melrose Group assets and liabilities are shown below:

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

These assets and liabilities are funded by:

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

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

Finance Director's review
Continued

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

These are discussed in turn below.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Finance Director's review

Continued

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

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

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

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

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

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

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

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

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

Contract and warranty risk management

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

Commodity cost risk management

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

Going concern

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

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

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

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

Geoffrey Martin
Group Finance Director
4 March 2021

Longer-term viability statement

In accordance with provision 30 of the UK Corporate Governance Code, the Directors have assessed the prospects of the Company over a longer period than the 12 months required by the "Going Concern" provision. A period of three years is believed to be appropriate for this assessment since this is consistent with the Group's financing cycle, whereby on average the Group has refinanced debt in line with this timescale, usually as a result of acquisition or disposal activity.

The Directors confirm that they have a reasonable expectation that the Group will continue in operation and meet its liabilities, as they fall due, up to December 2023.

The Directors' assessment has been made by reference to the Group's financial position as at 31 December 2020, its prospects, the Group's strategy, the Board's risk appetite and the Group's principal risks and their management, all of which are described in the Strategic Report.

The Directors' assessment of the Group's viability is underpinned by a paper prepared by management. The paper is supported by comprehensive and detailed analysis and modelling. The model underpinning this statement is stress-tested, proven and is frequently used by management when determining working capital requirements for transactions and corporate restructuring. The main assumptions included in the model relate to forecast revenue, operating margin and cash generation. The model includes three years of forecast data from the Group's business assets and incorporates agreed sensitivities for economic risk (impacting revenue and margins to reduce the rate of recovery currently being forecast), foreign exchange risk (impacting net debt and assuming adverse movements in foreign exchange rates) and liquidity risk (impacting net debt and assuming a deterioration in working capital), each of which have been considered both individually and in combination by the Board, together with expected achievable mitigating actions from the working capital model to create severe, but plausible, scenarios. These scenarios sensitise the main assumptions noted above, considering the medium term impact of the COVID-19 pandemic, and also consider relevant cross-border trade risk including in respect of the UK's exit from the EU.

In preparing this statement, the following qualifications and assumptions are made:

(i) the viability model is based on the Group as at the date of this Annual Report, with no consideration of any further acquisitions or future disposals of continuing businesses. We note future acquisitions would be based on the same proven business model applied previously, with related bank debt and equity raised to support the acquisition with sufficient headroom to cover business risks; and

(ii) financing arrangements and bank covenant testing are in line with the current facility, renegotiated in the year, which is committed for some of the period under review. There is a high expectation that when the Group refinances its £450 million bond maturing in September 2022 and its multi-currency revolving credit facility, before January 2023, it will have sufficient headroom above covenants and in its liquidity to continue in operation.

Risk management

The Board recognises that operating in a dynamic and rapidly evolving commercial environment requires a pragmatic, robust and responsive risk management framework comprising policies, visibility and controls that change with the business and provide management with a comprehensive view of the Group's risk profile at any given time, enabling risk to be identified, assessed and managed.

Risk management responsibilities

The Board, having overall responsibility for risk management, has approved a formalised but pragmatic Group risk management framework.

Board Overall responsibility for risk management	• Agrees the Group's risk management strategy and defines its risk appetite • Reviews reports and recommendations from the Melrose senior management team and the Audit Committee on risk governance and risk processes and controls • Determines the nature and extent of the Group's principal risks and regularly discusses and assesses them throughout the year with the Melrose senior management team to determine the likelihood of those risks materialising and how they should be managed or mitigated • Maintains oversight of principal risks and mitigation plans including cyber security and fraud risk • Promotes an appropriate risk management culture and rewards system within the Group in order to maintain sound risk management and internal control systems	**Top down** At the Group level, risk oversight and assessment
Audit Committee Monitors the Group's internal financial control processes	• Monitors, oversees and reviews the effectiveness of the Group's internal controls and risk management systems and processes • Supports the Board in monitoring risk exposure against risk appetite	
Melrose senior management and business unit senior managers	• Set the risk management processes and controls • Agree how the principal risks should be managed or mitigated to reduce the likelihood of their incidence or impact • Consider actual and emerging risks • Oversee and challenges risk mitigation plans and support the legal and compliance teams within the business units	**Bottom up** Risk exposure identification and assessment at the business unit level
Operational managers and financial controllers	• Risk identification, assessment and monitoring at the business unit level • Implementing, reviewing and continually monitoring compliance with risk mitigation plans and controls • Embedding risk awareness and culture throughout the business	

The Board's view of the Group's principal risks and uncertainties is detailed in the table on pages 46 to 53.

Risk management strategy and framework

The objectives of the Directors and Melrose senior management include safeguarding and increasing the value of the businesses and assets of the Group for stakeholders as a whole. Achievement of these objectives requires the development of policies and appropriate internal control frameworks to ensure the Group's resources are managed properly, and for key risks to be identified and mitigated where possible.

The Board recognises that it is ultimately responsible for determining the nature and extent of the principal risks it is willing to take in the pursuit of its strategic objectives. It also recognises the need to define a risk appetite for the Group, to maintain sound risk management and internal control systems, and to monitor its risk exposures and mitigation measures to ensure that the nature and extent of risks taken by the Group are aligned with, and proportionate to, its strategic objectives.

The Group operates on a decentralised basis and the Board has established an organisational structure with clear reporting procedures, lines of responsibility and delegated authority, as depicted in the diagram above. Consistent with this, the Group operates a top-down, bottom-up approach to risk management, comprising Board and Melrose senior management oversight coupled with bottom-up risk management embedded in the day-to-day activities of its individual businesses.

The Board confirms that there is an ongoing process for identifying, evaluating, tracking and managing the principal risks faced by the Group and that these systems, which are subject to regular monitoring and review, have been in place for the year under review up to the date of approval of this Annual Report and financial statements. The Board further confirms that the systems, processes and controls that are in place accord with the guidance contained in the Financial Reporting Council's "Guidance on Risk Management, Internal Control and Related Financial Business Reporting" and the UK Corporate Governance Code (the "Code").

The Audit Committee monitors, oversees and reviews the effectiveness of the risk management and internal control processes implemented across the Group, through regular updates and discussions with management and a review of the key findings presented by the external and internal auditors. The Board is responsible for considering the Audit Committee's recommendations and ensuring implementation by divisional management of those recommendations it deems appropriate for the business. A description of the Audit Committee's activities during the year on risk management can be found on pages 104 to 105.

The management team of each business unit is responsible for monitoring business level risk and implementing and maintaining an

Risk management framework

- **Identification** Financial and non-financial risks recorded in controlled risk registers
- **Evaluation** Risk exposure reviewed and risks prioritised
- **Mitigation** Risk owners identified and action plans implemented
- **Analysis** Risks analysed for impact and probability to determine gross exposure
- **Review and monitoring** Robust mitigation strategy subject to regular and rigorous review

effective risk and control environment within their respective business unit as part of day-to-day operations, in line with the Group risk management framework and internal control systems determined by the Board. The CEO and senior executive team of each division are responsible for, and report to the Melrose senior management team in respect of, specific and ongoing risks related to their respective business division, which are reported formally to the Audit Committee on an annual basis. In reviewing the process following the disruption caused by COVID-19, the Audit Committee shall receive a formal risk management report on a biannual basis, commencing in 2021, in addition to their regular receipt of updates from the Melrose senior management team on material items that arise relating to principal Group risks.

During the year under review, in accordance with provisions 28 and 29 of the Code, the Board continued to monitor the effectiveness of the Group's risk management and internal control systems. The Board concluded that the Group's risk management and internal control systems and processes were operating effectively. Follow-up actions in respect of progress and improvement in relation to financial controls are further discussed in the Audit Committee report.

In 2019, the Melrose senior management team supplemented the Group's enterprise risk management programme by building and implementing a data-driven Group reporting dashboard to automate the aggregation and reporting of Group risks, in conjunction with ongoing divisional risk reporting and advice from external risk management consultants. This marked a significant step forward in the Group's journey towards enhancing both divisional management's risk reporting transparency, and the Board's visibility of the Group's principal risks, to enable an increasingly robust assessment of each business's risk profile and their impact on the Group risk profile as a whole. In 2020, the dashboard's reporting output was further enhanced to provide the Audit Committee with additional detail and trend analysis compared to each division's respective key industries, further visibility on the significance of key divisional risks, and greater illustration of each division's risk appetite, to facilitate the Audit Committee's monitoring, oversight and review of the effectiveness of the Group's internal controls and risk management systems and processes.

Risk appetite

The Board has undertaken an exercise to consider its risk appetite across a number of key business risk areas. The results of this review indicate the relative appetite of the Board across the risk factors at a specific point in time. Any material changes in risk factors will impact the Board's assessment of its risk appetite.

The Board has a higher risk appetite towards its strategic risks, with a balanced appetite towards operational and commercial risk, and macro-economic and political risk. The Board seeks to minimise all health and safety risks and has a low risk appetite in relation to legal, compliance and regulatory risk. Similarly, a conservative appetite is indicated by the Board with respect to pension and finance-related risk and information technology cyber risk.

The results of the risk appetite review will support the Board's decision-making processes during 2021. The Board undertakes a review of its risk appetite at least annually.

Risk management actions

During 2020, the Board continued to deliver on the key management priorities identified in the 2019 review across the Group. Risk owners continued to take steps to mitigate the risk exposures across the Group, supported by specific actions undertaken to improve enterprise risk management across the Group during the year, as follows:

- reviewing and reaffirming the Board's risk appetite;
- monitoring the implementation of the risk management governance framework across all business units. This framework defines the Melrose principles for risk management and sets the standards for the identification, evaluation, prioritisation, recording, review and reporting of risks and their management or mitigation throughout the organisation;
- continuing to enhance Melrose risk register methods, dashboard reporting outputs, and risk profile mapping application throughout the Group. These provide the Board with greater levels of detail and visibility on the risk management systems and processes in place, and illustrate each principal risk facing the Group from both a gross risk (pre-mitigation) and net risk (post-mitigation) position. The risk mapping application provides Directors with a clear risk profile for the Group and enables the Board to determine the degree to which its profile is aligned with its risk appetite;
- reviewing and improving the Group's processes, data extraction and consolidation, and trend analysis around the assessment of principal risks and the ongoing monitoring and reporting of the Group's risk management performance; and
- augmenting the quarterly IT governance assessment for all sites across the Group, which enables clarity and consistency in the assessment of IT and cyber matters that are appropriate for the stage and sophistication of the Group's businesses, through desktop reviews of those quarterly assessments conducted by Ernst & Young, supported by a site visit verification plan that, whilst disrupted by COVID-19 travel restrictions during 2020, remains a key priority for the Group in 2021.

Assessment of principal risks

During the year, the Board undertook a robust, in-depth and comprehensive assessment of the emerging and principal risks facing the Group and specifically those that might threaten the delivery of its strategic business model, its future performance, solvency or liquidity.

A summary of the principal risks and uncertainties that could impact on the Group's performance is shown on pages 46 to 53. Further information detailing the internal control and risk management policies and procedures operated within the Group is shown on pages 101 to 102 of the Corporate Governance report.

Risk management priorities for 2021

Continual improvements were made during 2020 in respect of the Group's risk management processes. However, the Board recognises that Melrose cannot be complacent. In 2021, management will continue to focus on refining the risk management framework and further embedding a culture of effective risk management across the Group to ensure that risks and opportunities are identified and managed, to support the delivery of long-term value creation.

Further resources will continue to be devoted to strengthening the mechanisms for providing independent assurance and objective trend analysis on the effectiveness of the Group's risk management governance, processes and controls. IT cyber risk reporting will continue to be strengthened, and external cyber security advisors will continue to enhance their review findings from the ongoing internal assessments, validate results, and enable an enhanced layer of objective site review to bolster the Group's identification of emerging cyber risks, and deployment of appropriate mitigation actions.

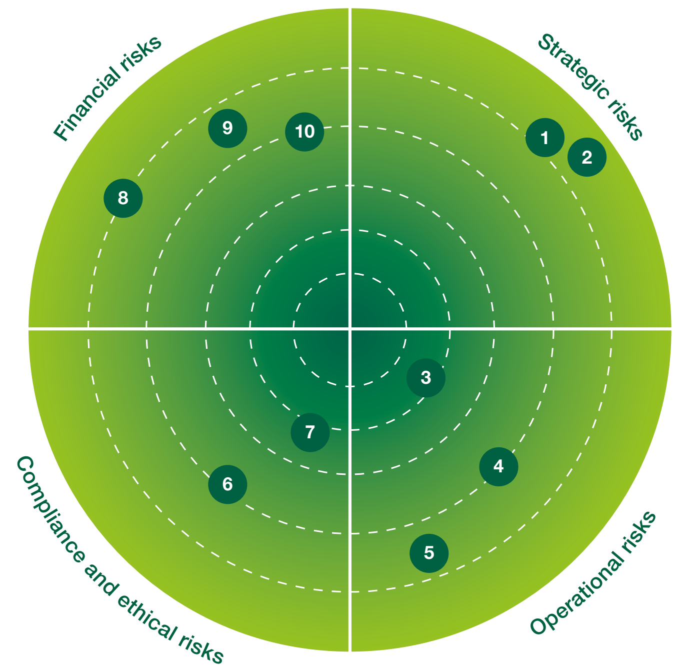
Strategic risk profile

A risk management and internal controls framework is in place within the Group, which is continually reviewed and adapted where necessary to reflect the risk profile of the Group and to continue to ensure that such risks and uncertainties can be identified and, where possible, managed suitably.

Each business unit maintains a risk register which is aggregated into an interactive data-driven dashboard reporting tool, to facilitate review by the Melrose senior management team, the Audit Committee and the Board.

Strategic risk profile

Our updated view of the Group's strategic risk profile is shown below.
The residual risk scores have been calculated on a post-mitigation basis.



No.	Risk rating	Risk title	Risk trend since last Annual Report	
1	Moderate	Acquisition of new businesses and improvement strategies	No change	2017 2018 2019 2020
2	Moderate	Timing of disposals	No change	2017 2018 2019 2020
3	Moderate	Economic and political	Increase	2017 2018 2019 2020
4	Moderate	Commercial	Increase	n/a 2017 2018 2019 2020
5	Moderate	Loss of key management and capabilities	No change	2017 2018 2019 2020
6	Moderate	Legal, regulatory and environmental	No change	2017 2018 2019 2020
7	Moderate	Information security and cyber threats	Increase	2017 2018 2019 2020
8	Moderate	Foreign exchange	No change	2017 2018 2019 2020
9	Moderate	Pensions	Decrease	2017 2018 2019 2020
10	Moderate	Liquidity	No change	2017 2018 2019 2020

Risk rating

Moderate impact

Likelihood

Unlikely → Likely

Strategic risks

Risk 1

Acquisition of new businesses and improvement strategies

Description and impact

The success of the Group's acquisition strategy depends on identifying available and suitable targets, obtaining any consents or authorisations required to carry out an acquisition, and procuring the necessary financing, be this from equity, debt or a combination of the two. In making acquisitions, there is a risk of unforeseen liabilities being later discovered which were not uncovered or known at the time of the due diligence process, particularly in the context of limited access in public bids. Further, as per the Group's strategy to buy and improve good but underperforming manufacturing businesses, once an acquisition is completed, there are risks that the Group will not succeed in driving strategic operational improvements to achieve the expected post-acquisition trading results or value which were originally anticipated, that the acquired products and technologies may not be successful, or that the business may require significantly greater resources and investment than anticipated. If anticipated benefits are not realised or trading by acquired businesses falls below expectations, it may be necessary to impair the carrying value of these assets. The Group's return on shareholder investment may fall if acquisition hurdle rates are not met. The Group's financial performance may suffer from goodwill or other acquisition-related impairment charges, or from the identification of additional liabilities not known at the time of the acquisition.

Mitigation

- Structured and appropriate due diligence undertaken on potential new targets where permitted and practicable.
- Focus on acquisition targets that have strong headline fundamentals, high-quality products, and leading market share but which are underperforming their potential and ability to generate sustainable cash flows and profit growth.
- Hands-on role taken by executive Directors and other senior employees of the Group.
- Development of strategic plans, restructuring opportunities, capital expenditure, procurement and working capital management.
- Proper incentivisation of operational management teams to align with Melrose strategy.

Responsibility	Executive management(1)
Risk trend	→

Trend commentary

Following the acquisition of GKN in 2018, the Group remains focused principally on improvement. The impact of COVID-19 has interrupted the timing of some improvement plans, but these are continuing at pace. Although no large acquisitions were made in 2020, the Group remains open to potential new opportunities.

Strategic priorities Buy Improve

(1) Comprises executive Directors and Melrose senior management.

Risk 2

Timing of disposals

Description and impact

In line with our strategy and depending where the Group is within the "Buy, Improve, Sell" cycle, the expected timing of any disposal of businesses is considered as a principal risk which could have a material impact on the Group strategy and performance. Further, due to the Group's global operations, there may be a significant impact on the timings of disposals due to political and macro-economic factors. Depending on the timings of disposals and the nature of the businesses' operations, there may be long-term liabilities which could be retained by the Group following a disposal. Insufficient allowance for such retained liabilities may affect the Group's financial position.

Mitigation

- Directors are experienced in judging and regularly reviewing the appropriate time in a business cycle for a disposal to realise maximum value for shareholders.
- Each disposal is assessed on its merits, with a key focus on a clean disposal.

Responsibility	Executive management(1)
Risk trend	→

Trend commentary

Although global M&A markets continue to experience uncertainty, there remain opportunities for value realisation, and a formal sale process has recently been commenced for the Nortek Air Management division. The process remains highly uncertain, but the division's outstanding recent performance will translate into a good outcome for the businesses and our shareholders. Some non-core businesses were sold or placed under strategic review during 2020. However, management continues to remain disciplined and there is no obligation to sell before it is appropriate to do so.

Strategic priorities Sell

Risks and uncertainties
Continued

Operational risks

Risk 3

Economic and political

Description and impact
The Group operates, through manufacturing and/or sales facilities, in numerous countries and is affected by global economic conditions. Businesses are also affected by government actions and the willingness of governments to commit substantial resources. Current global economic and financial market conditions have recently been characterised by high levels of volatility and uncertainty. There has been widespread disruption to production and trading environments caused by the COVID-19 pandemic, in particular a sharp market decline in the aerospace sector due to global travel restrictions. Fluctuation in commodity prices, the potential for a significant and prolonged global downturn and uncertainty in the political environment, may materially and adversely affect the Group's operational performance and financial condition, and could have a significant impact on the timing of acquisitions and disposals. These factors may also materially affect customers, suppliers and other parties with which the Group does business. Adverse economic and financial market conditions may cause customers to terminate existing orders, to reduce their purchases from the Group, or to be unable to meet their obligations to pay outstanding debts to the Group. These market conditions may also cause our suppliers to be unable to meet their commitments to the Group or to change the credit terms they extend to the Group's businesses.

Since the UK left the EU on 31 January 2020, uncertainty has continued in the UK regarding the nature and impact of the UK's future trading relationship with the EU and other international trading partners with which the UK intends to establish new terms on which to trade, and what this will mean for business and the UK economy.

The impact of the COVID-19 pandemic is a significant risk to the global economy. Each of the Group's businesses and their respective production and market geographies are impacted by the COVID-19 pandemic to various extents, with the most common impacts across the Group during 2020 being the temporary reduction of manufacturing capacity and reduced requirements due to lockdown measures and international travel restrictions. The Board and the Melrose senior management team continue to regularly monitor the impact of the pandemic on the Group with particular focus on the potential for staff shortages, production delays and supply chain disruption.

A significant amount of the Group's revenue is generated from operations located in North America, which during 2020 continued to experience challenging tariffs relating to the US/China trade war and uncertainty related to the US presidential election. The US has also required close monitoring related to the expected short to medium-term impact of potential changes to international trading relationships following the conclusion of a definitive future trade deal between the UK and the EU. The Group's exposure to such US trade risk factors is inherently mitigated by its manufacturing footprint across the UK and European-based GKN Aerospace and GKN Automotive divisions. Further, the Group's businesses operating in North America continue to take regular specific actions to mitigate the impact of new relevant North American tariffs and changes to international trading regulations by engaging with the relevant authorities prior to and after any such changes are implemented.

Whilst the long-term impact of Brexit, COVID-19, and tariff wars are not isolated as principal risks to the Group as a whole, they present potential risks that the business units continue to monitor and assess closely, particularly in the context of potential changes to travel and working restrictions, and the cross-border trade and regulatory environments in which the business units operate. The Board continues to assess and review the potential impact of these evolving risks.

(1) Comprises executive Directors and Melrose senior management.

Mitigation
- Regular Board meetings and business review meetings were supplemented by weekly meetings of the Board and weekly cash management meetings during the initial height of the COVID-19 pandemic during the second and third quarters of 2020. As the initial disruption subsided in the third quarter, these additional meetings moved to fortnightly, whilst the Board continued to receive key financial information on a weekly basis. The increased frequency of meetings at Board level enabled the Board to discuss and increase their monitoring and oversight of the impact of macro-political events on the Group on a regular basis, including national and regional lockdowns, material working pattern changes, PPE supplies and distribution, and the business units' ongoing assessment of and/or use of and paying back of national support schemes where deemed appropriate.
- Regular monitoring of order books, cash performance, cost control and other leading indicators, to ensure the Group and each of its businesses could respond quickly to adverse trading conditions. This included the identification of cost reduction and efficiency measures.
- Bank financing is readily available to the Group from its supportive banking syndicate. This support has proven to be available to the Group even during periods of unprecedented turmoil that was experienced in 2020 due to the global pandemic.
- Assessment of and/or use of national support schemes where deemed appropriate in the context of COVID-19 disruption.
- Short-term inventory buffers are regularly reviewed and assessed to minimise the impact of further lockdown restrictions due to COVID-19, and the initial impact of Brexit on import costs and tariffs and border disruption.
- Sales from the EU to the UK within the GKN Aerospace and GKN Automotive divisions are frequently on ex-works terms and therefore a cost to customers. This continued to be reviewed during 2020 in light of the then ongoing Brexit negotiations and the subsequent ongoing trading terms between the UK and the EU.
- Strong customer relationships built on long-term partnerships often with plants in close proximity, technical excellence and quality.
- Planning for potential discussions in respect of increased tariff costs that materialise following the final Brexit deal between the UK and the EU.
- The Group remains agile, diversified and well positioned to deal with any short-term uncertainty in the UK.

Responsibility	Executive management(1)
Risk trend	↑

Trend commentary
There were unprecedented levels of volatility and uncertainty during 2020 primarily as a result of COVID-19.

The Melrose senior management team continues to actively engage with the business unit executive teams to track the potential impacts of further lockdowns or tiered restrictions aimed at curbing the impact of COVID-19, as well as the potential impacts of Brexit and the possibility of future tariffs. The Melrose senior management team engages actively with those who are working on the relevant impact assessments and mitigation actions, and reports the material findings to the Board. The Melrose senior management team monitors key issues with the divisional management teams including the impact of geopolitical uncertainty on order books, cash generation, legal and regulatory threats and other key operational and commercial indicators, to ensure the Group and each of its businesses can respond appropriately to adverse trading conditions. Tactics for mitigating the potential impact of geopolitical uncertainty include identifying cost reduction and operational efficiency measures.

The Board notes that economic uncertainty can depress business valuations and this may increase the number of potential acquisition opportunities for Melrose.

Strategic priorities Buy Improve Sell

Risk 4

Commercial

Description and impact
The Group operates in competitive markets throughout the world and is diversified across a variety of industries and production and sales geographies. This provides a degree of Group-level impact mitigation from the potential commercial challenges and market disruptions that face each of the divisions. However, the widespread disruption caused by COVID-19 has heightened the Group's exposure to supply chain and end-market commercial risk.

Each division is exposed to particular commercial and market risks, which are primarily accentuated where customer/competitor concentration is high within their respective market segments.

Melrose operates a decentralised control and management structure which empowers divisional management teams to take full responsibility for planning, mitigating, navigating and responding to the specific commercial risks and challenges facing their respective businesses. The Melrose senior management team monitors the aggregated impact of such risks and provides active support and challenge to the divisional management teams in fulfilling their responsibilities.

Common commercial risk areas that potentially affect a large proportion of the Group's businesses include those related to production quality assurance, health and safety performance, customer concentration and uncertainties related to future customer demand, onerous customer and supplier contracts, the impact of increased competitive pressures on the maintenance/improvement of market share, potential disruptions to supply chains and increases to the price of raw materials, technological innovation and market disruption, and the performance and management of programme partners ("Common Commercial Risks").

In 2020, Common Commercial Risks increased due to the impact of the global pandemic, which affected a number of areas including supply chains, production scheduling, factory closures, customer demand rates, and freight.

Mitigation
- The Group continued to actively invest in research and development activities in 2020 to augment its platforms for future product expansion, quality improvements, customer alignment and achieving further production efficiencies. Details about some of the Group's research and development activities are provided in the Sustainability report on pages 58 to 87.
- Health and safety awareness initiatives and performance enhancements continued to be implemented in alignment with regulation, market practice and site-based risk assessments and requirements. In addition, in light of the COVID-19 pandemic, the Group has followed government guidance on hygiene and social distancing protocols, and coordinated the sourcing of PPE globally to ensure no disruptions.
- Since acquiring GKN, the Melrose senior management team has actively engaged with and supported the GKN businesses' divisional management executive teams in identifying embedded contractual and business conduct risks relating to key supply chain and production programme partners. Those management teams have continued to implement and direct a series of operational change management programmes to mitigate the risks they have identified.
- The Melrose senior management team, in collaboration with Ernst & Young, continues to enhance the Board and Audit Committee's visibility of the Group's Common Commercial Risks through the use of the Group reporting dashboard to aggregate and report numerous Common Commercial Risks across each of the Group's divisions.
- Throughout the COVID-19 pandemic, the rate and intensity of business unit reporting was substantially increased. This ensured business unit management and the Melrose senior management team had timely access to detailed and accurate information on the trading performance of the Group, which enabled informed and quick decision-making.

Responsibility	Executive management(1)
Risk trend	↑

Trend commentary
The Melrose senior management team actively engages with the divisional executive management teams to track, monitor and support strategic planning activities and impact mitigation assessments in respect of ongoing commercial risks. Particular focus is placed on certain GKN Aerospace and GKN Automotive end markets where customer and/or competitor concentration is high and heavier reliance is placed on supply chain efficiency and programme partner management. The divisional CEOs report material updates directly to members of the Melrose senior management team which maintains a number of contact points throughout the Group to increase awareness.

Strategic priorities Improve

(1) Comprises executive Directors and Melrose senior management.

Melrose Industries PLC Annual Report 2020

Risks and uncertainties

Continued

Operational risks – continued

Risk 5

Loss of key management and capabilities

Description and impact

The success of the Group is built upon strong management teams. As a result, the loss of key personnel could have a significant impact on performance, at least for a time. The loss of key personnel or the failure to plan adequately for succession or develop new talent may impact the reputation of the Group or lead to a disruption in the leadership of the business. Competition for personnel is intense and the Group may not be successful in attracting or retaining qualified personnel, particularly engineering professionals.

Mitigation

- Succession planning within the Group is coordinated via the Nomination Committee in conjunction with the Board and includes all Directors and senior Melrose employees. In line with the Group's decentralised structure, each divisional CEO, in consultation with the Chief Executive, is responsible for the appointment of their respective executive team members, with disclosure to the Nomination Committee via the Melrose senior management team.
- The Company recognises that, as with most businesses, particularly those operating within a technical field, appointments are dependent on Directors and employees with particular managerial, engineering or technical skills. Appropriate remuneration packages and long-term incentive arrangements are offered in an effort to attract and retain such individuals.

Responsibility	Executive management(1)
Risk trend	→

Trend commentary

Succession planning remains a core focus for the Nomination Committee and the Board. Reviewing the succession planning arrangements of the Board as a whole, together with a review of the Melrose senior management team, will remain an area of particular focus in 2021, as well as maintaining oversight of business unit succession planning.

Strategic priorities Buy Improve Sell

(1) Comprises executive Directors and Melrose senior management.

Compliance and ethical risks

Risk 6

Legal, regulatory and environmental

Description and impact

Considering the breadth, scale and complexity of the Group, there is a risk that the Group may not always be in complete compliance with laws, regulations or permits. The Group could be held responsible for liabilities and consequences arising from (i) past or future environmental damage, including potentially significant remedial costs; (ii) employee matters including liability for employee accidents in the workplace or consequences of environmental liabilities, which may be susceptible to class action law suits, particularly but not exclusively with respect to Group businesses operating in North America; (iii) restrictions arising from economic sanctions, export controls and customs, which can result in fines, criminal penalties, adverse publicity, payment of back duties and suspension or revocation of the Group's import or export privileges; and (iv) product liability claims, which can result in significant total liability or remedial costs, particularly for products supplied to large volume global production programmes spanning multiple years, for example in the aerospace and automotive industries, or to consumer end markets, for example in the air management industry. There can also be no assurance that any provisions for expected environmental liabilities and remediation costs will adequately cover these liabilities or costs.

The Group operates in highly regulated sectors, which has been accentuated by the GKN acquisition. In addition, new legislation, regulations or certification requirements may require additional expense, restrict commercial flexibility and business strategies or introduce additional liabilities for the Group or the Directors. For example, the Group's operations are subject to anti-bribery and anti-corruption, anti-money laundering, competition, anti-trust and trade compliance laws and regulations. Failure to comply with certain regulations may result in significant financial penalties, debarment from government contracts and/or reputational damage, and may impact our business strategy.

We purchase businesses that are underperforming their potential with respect to their financial, operational and sustainability performance. Inherent in the nature of the manufacturing businesses we acquire is that they often operate in industries that are the hardest to decarbonise. Group sustainability performance and ratings will fluctuate during our investment cycle as we acquire new businesses in need of improvement, and sell businesses that we have improved.

Mitigation

- Regular monitoring of legal and regulatory matters at both a Group and business unit level. Consultation with external advisors where necessary.
- Group-wide standard and enhanced application to trade authorisation procedures are in place and regularly reviewed against the ever-changing global trade compliance landscape, supported by access to external trade compliance legal and regulatory specialists and electronic counterparty screening systems.
- Our businesses are validated and certified in respect of quality management, environmental management and health and safety with the appropriate bodies including ISO and BS OHSAS, where relevant to their operations. The Group's businesses are either already compliant with or working towards timely compliance with new and upcoming standards. This includes Group businesses that are currently certified to BS OHSAS 18001 and are actively driving towards full transition to ISO 45001:2018.
- With Melrose support, each business invests in and implements appropriate systems and processes to manage their impact on the environment, and continually reviews these in line with evolving expected practices. The executive management team of each business regularly reviews any significant climate-related issues, risks and opportunities related to the business. These reviews consider the level of climate-related risk that the business is prepared to take in pursuit of its business strategy and the effectiveness of management controls in place to mitigate climate-related risk. Any identified risks are discussed with the Melrose senior management team and escalated to the Board where necessary.
- In line with our decentralised model, our businesses have frameworks in place for identifying principal risks and opportunities appropriate to their business and stakeholders, which include climate-related risks. Each business takes an appropriately tailored approach to climate-related initiatives that suits their requirements, and operational and market environments, as well as reflecting their maturity in this area at the time of becoming part of the Group.
- The Board sets a leading example in sustainability, and holds each business and their management teams accountable for their progress, and provides them with a platform to absorb the Group's best practices, to accelerate their and others' progress.
- The Melrose senior management team works with the businesses' executive teams, to set meaningful sustainability targets, alongside financial metrics, and Melrose provides the investment to achieve them. The businesses subsequently identify, monitor, and manage the specific environmental risks that affect their operating and market environments.
- The Board with the support of the Melrose senior management team reviews the annual reports on energy usage and greenhouse gas emissions within each business, and provides support and investment to drive improvements within their operations through more efficient use of electricity, fuel and heat, including by increasing the proportion of renewable energy where commercially viable, and by implementing other climate-positive actions such as sustainable transport initiatives for employees.
- The Board with the support of the Melrose senior management team spends time listening to the Group's key stakeholders to enable informed strategic decisions and to deliver on their needs.
- A robust control framework is in place, underpinned by comprehensive corporate governance and compliance procedures at both a Group and business unit level, including utilisation of third party verification providers.
- Where possible and practicable, due diligence processes during the acquisition stage seek to identify legal, regulatory and environmental risks. At the business unit level, controls are in place to prevent such risks from crystallising.
- Any environmental risks that crystallise are subject to mitigation by specialist consultants engaged for this purpose. External consultants assist the Group in complying with new and emerging environmental regulations.
- Insurance cover mitigates certain levels of risk and the Group's insurers are instructed to carry out external audits of specified areas of legal and compliance risk including health and safety.

Responsibility	Executive management(1)
Risk trend	→

Trend commentary

Each business has a fully developed legal function, headed by their respective General Counsel reporting to their executive management team, and are properly staffed and supported by external advisors where necessary or helpful to ensure ongoing compliance in the jurisdictions in which they operate across the globe. This is augmented by central oversight from the Melrose legal team and robust annual reviews.

The Board reviews its assessment of the Group's material sustainability issues annually, and is currently establishing a Group internal sustainability reporting and performance function to support the business units. During the coming year, the Board with the support of the Melrose senior management team will publish an assessment of how Melrose and its businesses are mitigating climate change risks aligned with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), and setting targets in line with the UN Sustainable Development Goals.

Strategic priorities Improve

(1) Comprises executive Directors and Melrose senior management.

Melrose Industries PLC Annual Report 2020

Risks and uncertainties
Continued

Compliance and ethical risks – continued

Risk 7
Information security and cyber threats

Description and impact
Information security and cyber threats to our systems are an increasing priority across all industries and remain a key UK Government agenda item.

Like many businesses, Melrose recognises that the Group may have a potential exposure in this area. Potential exposure to such risks remains high due to the scale, complexity and public-facing nature of the Group. In addition, Melrose recognises that the inherent security threat is considered highest in GKN Aerospace where data is held in relation to civil aerospace technology and controlled military contracts.

Mitigation
- Management work with the leaders of each business and external security consultants to assess the Group's increased exposure to cyber security risk and to ensure appropriate mitigation measures are in place for the Group.
- During 2020, Melrose continued to monitor and enhance its information security strategy and risk-based governance framework with all businesses within the Group. The framework follows the UK Government's recommended steps on cyber security. This strategic management approach has delivered risk profiling capabilities by business and the enablement of mitigation plans to be developed for each business to reduce their exposure to cyber risk.
- The progress of each business is measured against the information security strategy and is monitored on a quarterly basis. Data is also externally reviewed quarterly by Ernst & Young, who will be augmenting their review in 2021 with a mix of virtual and onsite assurance visits.

Responsibility	Executive management(1)
Risk trend	↑

Trend commentary
Information security and cyber threats are an increasing priority across all industries. The COVID-19 pandemic has increased online traffic, reduced physical contact, and created additional new threats to all of our businesses requiring increased attention. Cyber security breaches of the Group's IT systems could result in the misappropriation of confidential information belonging to it or its customers, suppliers or employees. In response to the increased sophistication of information security and cyber threats, the Group has worked, and continues to work, with external security companies to monitor, improve and refine its Group-wide strategy to aid the prevention, identification and mitigation of any present and future threats.

Strategic priorities Improve

(1) Comprises executive Directors and Melrose senior management.

Financial risks

Risk 8
Foreign exchange

Description and impact
Due to the global nature of operations and volatility in the foreign exchange market, exchange rate fluctuations have, and could continue to have, a material impact on the reported results of the Group.

The Group is exposed to three types of currency risk: transaction risk; translation risk; and the risk that when a business that is predominantly based in a foreign currency is sold, it is sold in that foreign currency. The Group's reported results will fluctuate as average exchange rates change. The Group's reported net assets will fluctuate as the year-end exchange rate changes.

Mitigation
- The Group policy is to protect against the majority of foreign exchange risk which affects cash, by hedging such risks with financial instruments.
- The businesses are protected against being over-hedged, due to short to medium-term reductions in forecasts, as the percentage of hedges compared to forecast foreign exchange exposures tapers over future periods.
- Protection against specific transaction risks is taken by the Board on a case-by-case basis.

Responsibility	Executive management(1)
Risk trend	→

Trend commentary
Group results are reported in Sterling but a large proportion of its revenues are denominated in currencies other than Sterling, primarily US Dollar and Euro. Sensitivity to the key currency pairs is shown in the Finance Director's review on pages 36 to 42.

Strategic priorities Buy Improve Sell

Risk 9
Pensions

Description and impact
Any shortfall in the Group's defined benefit pension schemes may require additional funding. As at 31 December 2020, the Group's pension schemes had an aggregate deficit, on an accounting basis, of £838 million (2019: £1,121 million). Changes in discount rates, inflation, asset values or mortality assumptions could lead to a materially higher deficit. For example, the cost of a buy-out on a discontinued basis uses more conservative assumptions and is likely to be significantly higher than the accounting deficit.

Alternatively, if the plans are managed on an ongoing basis, there is a risk that the plans' assets, such as investments in equity and debt securities, will not be sufficient to cover the value of the retirement benefits to be provided under the plans. The implications of a higher pension deficit include a direct impact on valuation, implied credit rating and potential additional funding requirements at subsequent triennial reviews. In the event of a major disposal that generates significant cash proceeds which are returned to the shareholders, the Group may be required to make additional cash payments to the plans or provide additional security.

Mitigation
- The Group's key funded UK defined benefit pension plans are closed to new entrants and future service accrual. Long-term funding arrangements are agreed with the Trustees and reviewed following completion of actuarial valuations.
- Active engagement with the Trustees on pension plan asset allocations and strategies.
- During the year the GKN Schemes 1-4 appointed a fiduciary manager which will allow more timely decisions to be made on changing investments as circumstances require. Also, investments can be spread across more asset classes which will reduce risk.

Responsibility	Executive management(1)
Risk trend	↓

Trend commentary
Although the risks are well understood, the deficit significantly reduced and funding plans for the GKN Schemes having already been agreed with the Trustees, the size of the gross liabilities as a proportion of the Group's net assets remains significant. During the period, gross liabilities increased as a result of changes in financial conditions. The increase was offset by increases in scheme assets arising from the return on investments and group contributions of £111 million. As a result of the deficit reduction during the period, the Trustees took action to better hedge risks associated with movements in inflation and interest rates, and to reduce investment risk. Accordingly, the volatility risk to the Group is reduced.

Strategic priorities Buy Improve Sell

(1) Comprises executive Directors and Melrose senior management.

Risk 10
Liquidity

Description and impact
The ability to raise debt or to refinance existing borrowings in the bank or capital markets is dependent on market conditions and the proper functioning of financial markets. As set out in more detail in the Finance Director's review on pages 36 to 42, the Group has term loans of US$960 million and £100 million and revolving credit facilities comprising US$2.0 billion, €0.5 billion and £1.1 billion.

In addition, the GKN net debt at acquisition included capital market borrowings across three unsecured bonds that totalled £1.1 billion. Two of these bonds – totalling £750 million – remain outstanding as at 31 December 2020 and further detail is provided in the Finance Director's review on pages 36 to 42.

The sudden and material impact of COVID-19 in 2020 has brought cash management into sharp focus. In line with the Group's strategy, investment is made in the businesses (capital expenditure and restructuring actions) and there is a requirement to assess liquidity and headroom when new businesses are acquired.

Mitigation
- To ensure it has comprehensive and timely visibility of the liquidity position, the Group conducts monthly reviews of its cash forecast, which are in turn revised quarterly.
- The Group operates cash management mechanisms, including cash pooling across the Group and maintenance of revolving credit facilities to mitigate the risk of any liquidity issues.
- The Group gained agreement from its lenders to a three-year extension, at the Group's option to be built into its multi-currency term loan denominated £100 million and US$960 million, exercisable at any time prior to 1 April 2021 that would extend the maturity date of the loan to 30 April 2024. Since the end of the current reporting period, this option has been exercised.
- The Group operates a conservative level of headroom across its financing covenants which is designed to avoid the need for any unplanned refinancing.
- As a result of COVID-19 the Group's banking syndicate agreed to amend its financial covenants during the year, covering the periods up to and including 31 December 2022, which provides significant headroom over the existing covenants.

Responsibility	Executive management(1)
Risk trend	→

Trend commentary
Whilst the Group maintains strong cash controls and forecasting processes, in light of the COVID-19 pandemic, management have driven a redoubling of efforts throughout the Group to increase visibility and certainty of cash flow information, robustness of cash controls, and cash-saving initiatives. These have been very successful and combined with the negotiation of covenant waivers with our supportive banking syndicate, the Group is satisfied that it has adequate resources available to meet its liabilities.

Strategic priorities Buy Improve

Melrose Industries PLC Annual Report 2020

Section 172 statement

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

Our purpose, strategy and values

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

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

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

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

SECTION 172(1) STATEMENT

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

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

Duty to promote the success of the Company

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

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

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

Our key stakeholders

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

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

Long-term decision making

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

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

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

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

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

Employees

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

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

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

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

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

Suppliers and customers

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

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

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

Shareholders

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

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

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

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

Environment and community

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

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

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

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

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

Government bodies

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

Corporate governance agencies and independent reporting bodies

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

Maintaining a reputation for high standards of business conduct

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

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

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

Acting fairly as between the Company's shareholders

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

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

Key Board decisions during 2020

We have outlined below some of the key decisions made by the Board over the year, explaining how the Directors engaged with stakeholders, and how stakeholder interests were considered over the course of the Board's decision-making.

Negotiation of Bank Covenant Waivers

One of the Board's first decisions at the start of the COVID-19 pandemic was to seek to reach an agreement with the Company's banking syndicate to temporarily waive certain covenants in the Group's overall banking arrangements, in order to provide the Group with flexibility to focus on cash generation and adapting the Group to the current market conditions.

The requested waivers allowed management to focus on cash generation without the restrictions previously agreed with the Group's lending banks, for a temporary period. There was a modest cash cost to secure this amendment, but there was no change to previously agreed interest rate calculations. The Board therefore considered this decision to be in the best interests of the Group's key stakeholders as it would mitigate the risk of the Group needing to seek any further waivers in the future, and therefore gave management the ability to focus on areas requiring more immediate action in light of the pandemic.

Melrose agreed amended arrangements with its banking syndicate in August 2020, including improved financial covenants to 31 December 2022. These amendments cover all of the Group's primary borrowing arrangements that contain financial covenants.

Shareholder Distributions

In light of the Board's focus on maintaining the Group's financial position, given the significant level of trading certainty initially posed by the pandemic, the Board felt that it must act prudently and conservatively in respect of payments to shareholders. As such, the Board determined not to pay the 2019 final dividend that was due to be paid in May 2020.

Melrose aims to provide shareholders with sustained returns through a combination of dividend income and special distributions following sales of businesses, operating a progressive dividend policy whenever the financial position of the Company, in the opinion of the Board, justifies the payment. Given the impact of the pandemic on the Group, the Board did not feel it was appropriate to pay a dividend to shareholders in 2020, being a further outflow of cash from the Group. The decision was effectively communicated to, and well understood by, shareholders.

We understand the importance of dividends to shareholders and the material impact of withdrawing dividends. The Board is very pleased to be able to propose to pay a final dividend to shareholders of 0.75 pence per share, subject to approval at the AGM on 6 May 2021.

Approval of the Melrose 2020 Employee Share Plan

The Board had consulted extensively with key stakeholders at the start of 2020 on the renewal of the Company's long-term incentive arrangements, in advance of the 2020 AGM. The uncertainty initially presented by the COVID-19 pandemic led the Board not to propose a resolution in relation to a new long-term incentive plan to follow the previous plan, which expired in May 2020 for no value. The Board continued to monitor the situation and, in autumn 2020, commenced a further round of consultation with key shareholders and other stakeholders on a revised proposal.

It is important for all stakeholders that management are properly incentivised to deliver exceptional returns for shareholders, a view that was expressed by shareholders during the consultation. The Board had to strike a balance between ensuring that management are incentivised to create exceptional value for shareholders, whilst ensuring that performance conditions are sufficiently challenging and stretching.

The Board determined to make certain adjustments to the original proposal, to reflect the impact of COVID-19 on the Group's businesses and likely performance of the Group over the three-year performance period of the plan. The revised proposal was presented to key shareholders and changes were incorporated into the final proposal as a direct result of these discussions, including additional adjustments to protect shareholders. The 2020 Employee Share Plan was approved by shareholders in January 2021 with a vote in favour of 82.64%.

Protecting Employees During the Pandemic

The Board is acutely aware of the need to keep all workers safe. This has always been a top priority, but gained a heightened focus in 2020 due to the COVID-19 pandemic. Given the industries in which the Group's businesses operate, ensuring that manufacturing sites were able to remain open – in compliance with regional regulations and government advice – was key, but it was clearly extremely important that any return to work was safe for all employees.

The Board took rapid and decisive action in response to the pandemic in order to keep employees safe. Designated task forces and steering committees were established by the businesses, which were assigned responsibility for assessing and managing risks and ensuring clear communication to key stakeholders about the COVID-19 pandemic. A Group-wide PPE procurement exercise was initiated in order to ensure that all businesses had requisite supplies of PPE, together with enhanced workplace cleaning measures and employee guidelines on safe working, as well as adjustments to usual work processes to ensure compliance with social distancing measures, to make sure that employees felt comfortable returning to work. The range of measures implemented across the Group are described in more detail in the Sustainability report on page 75.

Sustainability as a Matter of Strategic Importance

The Board produced its inaugural ESG report in 2019 to highlight the investment, support and encouragement provided to the Group's businesses to enable them to pursue relevant improvements in relation to sustainability, and the Board's recognition of the growing importance of supporting the Group's actions in this area, with enhanced disclosure. It has become clear that stakeholders are requiring more detailed and transparent disclosure, and in light of this, the Board looked at elevating sustainability as a matter of strategic importance for the Group.

External advisors were engaged to perform a peer review on sustainability reporting and to advise the Board on how to accelerate the Group's efforts in tackling material sustainability matters in the most efficient and appropriate way in light of Melrose's decentralised model, which does not fit a standard approach to reporting, yet in a way that is meaningful for all relevant stakeholders. The Board felt that in addition to the business unit strategies in this area, for which the Board will continue to provide its full support, it was important for Melrose to set its own targets and expectations on sustainability for businesses under Melrose ownership.

The Sustainability report on pages 58 to 87 demonstrates a significant gear change in the Board's efforts to provide detailed and transparent disclosure to all relevant stakeholders on this topic. Sustainability is also addressed elsewhere in this Annual Report where appropriate to other areas, such as governance and executive remuneration, highlighting the Board's view of sustainability as a matter that is relevant to all areas of business. The Board will endeavour to improve upon its disclosures and actions in this area each year.

Melrose provides the focus and investment to make our businesses sustainable and valuable, for the benefit of our stakeholders

Introduction

Following our inaugural ESG report last year, we have continued to embed our four Melrose sustainability principles within our businesses. This 2020 Sustainability report sets out the results of our material sustainability issues assessment, illustrates the alignment of the Melrose sustainability principles to the UN SDGs, and provides updated detail and case studies that demonstrate the efforts that our businesses have made to promote those principles and goals throughout 2020. Highlights include our:

- Further efforts made to continue to **embed sustainability** within our businesses.
- Additional investment in our businesses to make **products that are more sustainable and safer**, with a focus on helping our businesses' customers and their wider industries to support the transition to a net zero emissions economy by 2050.
- Progress towards **making the impact of our businesses' production activities more environmentally friendly**.
- Continued focus on **prioritising the health and safety of our employees and contractors**.
- Continued **investment in the wellbeing and skills development of our employees and the communities that they are part of**, including our efforts to **promote diversity**.
- **Further strengthening of our governance, risk management, and compliance framework**, and maintaining **strong ethical conduct and business practices** throughout the Group.

A focus on sustainability

Justin Dowley
Non-executive Chairman

Improving the sustainability performance of our businesses is central to our "Buy, Improve, Sell" strategy. We acquire good manufacturing businesses that are underperforming their potential from a financial, operational and sustainability perspective. We then invest heavily to improve their longer-term financial and operational performance in a sustainable manner, before identifying suitable new owners who will take them to the next stage of their development, generating significant value for our shareholders.

Inherent in the nature of the manufacturing businesses we acquire is that they often operate in the industries that are some of the most difficult to decarbonise. We provide the focus and investment that these businesses need to deliver significant financial returns and sustainability improvements for the benefit of our stakeholders. We work with our businesses to set meaningful sustainability targets, alongside financial metrics, and we provide the investment to achieve them. We set a positive example for our businesses and provide them with a platform to share Group best practices and accelerate the pace of change within their organisations, whilst influencing positive change within our other businesses.

By the very nature of our "Buy, Improve, Sell" strategy, our Group sustainability performance and ratings will fluctuate during our investment cycle as we acquire new businesses in need of improvement, and sell businesses that we have improved. By turning around the performance of those businesses under our ownership, we will have added value for the benefit of our stakeholders.

We redirect and refocus our businesses on helping their customers and key stakeholders tackle pressing climate change challenges in pursuit of transitioning to a net zero emissions economy by 2050. Through a combination of investment and oversight, we redirect and refocus our businesses to work closely with their customers to develop and deliver innovative product solutions that directly address society's most complex longer-term sustainability challenges.

Our efforts to improve our businesses are supported by a foundation of robust governance, risk management and compliance. We instil the highest standards of integrity, honesty, and transparency within the businesses we acquire, and we require them to demand the same of their supply chains. We also spend time listening to our key stakeholders so we can make more informed strategic decisions and deliver on their needs. This includes our employees, whose wellbeing and skills development is a key priority, as well as the communities in which our businesses operate.

We take our role as a responsible corporate citizen seriously by encouraging innovation and implementing measures to drive positive change and to proactively reduce the potential negative impact of our businesses' and our customers' operations on society and the planet.

Progress in 2020

In 2020 we delivered significant progress against our four overarching sustainability principles, which are: (i) to respect and protect the environment; (ii) to purposefully engage with key stakeholders to better understand and deliver on their expectations; (iii) to prioritise and nurture the wellbeing and skills development of employees and the communities that they are part of; and (iv) to exercise robust governance, risk management, and compliance. Despite the disruption caused by the COVID-19 pandemic, our businesses continued to excel in cultivating the technical capabilities required to provide innovative solutions to the emerging sustainability challenges that their customers face. We are already taking active steps to anticipate how climate change will affect our businesses and they, in turn, are investing in sustainable product development that will help their customers achieve their sustainability ambitions. Highlights in 2020 included the launch of a groundbreaking hydrogen propulsion project led by GKN Aerospace, which aims to deliver a hydrogen-powered aircraft with zero carbon emissions to the skies from as early as 2026, and GKN Automotive's continued market leadership in developing highly efficient all-wheel drive ("AWD") and eDrive systems that enable customers to improve fuel efficiency and reduce their carbon emissions.

Across the Group, we took further steps to implement a more comprehensive sustainability framework to support the execution of our "Buy, Improve, Sell" strategy. We refined our Group sustainability objectives and strengthened our controls, which included the development of a formal sustainability framework covering the following:

- completion of a materiality assessment;
- alignment to the UN Sustainable Development Goals (UN SDGs);
- establishment of a Group internal sustainability reporting and performance function to support our businesses;
- implementation of a refreshed Melrose Code of Ethics, applicable to all of our businesses; and
- refreshing our Group compliance policies and introducing a new Group-wide conflict minerals policy.

Actions for 2021

In executing our "Buy, Improve, Sell" strategy and effecting continuous, long-term improvement within our businesses, we recognise that our work is far from complete. We are committed to continuing to improve the contribution that our businesses make to sustainable development, and to further enhance our sustainability framework. Our plans for 2021 include:

- developing a multi-year sustainability action plan to embed sustainable performance targets within the Group which reflect our "Buy, Improve, Sell" strategy and our three to five-year investment cycle. We will disclose these performance targets in due course;
- further developing our sustainability management and governance structure, including our internal sustainability reporting capabilities and information capture across our businesses;
- commencing the process of reporting our sustainability performance under the Sustainability Accounting Standards Board (SASB);
- making our inaugural CDP (formerly the Carbon Disclosure Project) submission;
- publishing an assessment of how we are mitigating climate change risks in line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD); and
- setting targets in line with the selected UN SDGs that measure the contribution of our businesses to those goals.

Much of this work is already underway and we look forward to accelerating our progress during 2021.

J Dowley

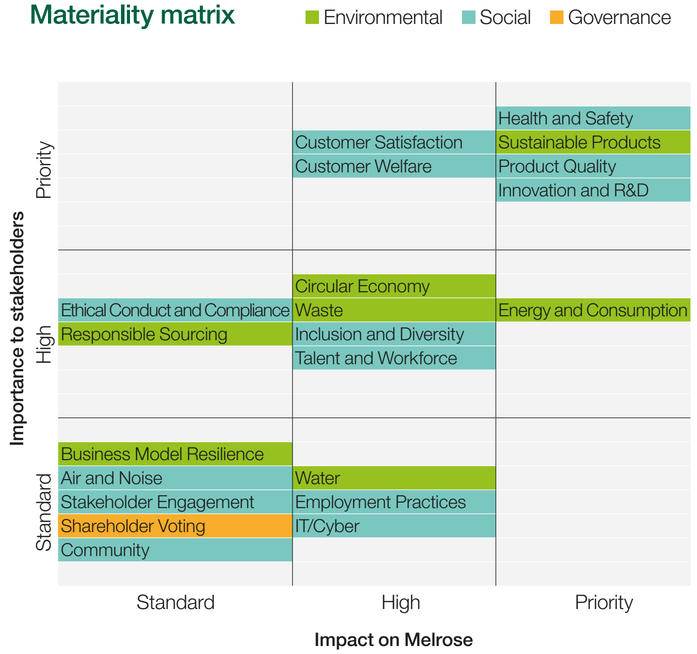
Justin Dowley
Chairman
4 March 2021

Embedding Sustainability

In 2020 we undertook a materiality assessment to identify the key sustainability issues that impact our ability to create value over time and are of most concern to our stakeholders. This process has helped prioritise the main sustainability topics that are impacted by our businesses' activities and has informed our Group strategy. We do not view these as isolated issues. We appreciate that they are often interconnected and recognise that a change to one can have an impact on others.

Our materiality assessment included a review of relevant reporting frameworks and standards, peer group benchmarking across our businesses' respective Aerospace, Automotive, Materials Science and Industrial peers, direct consultation with the CEOs and executive management teams of our largest businesses, integrating feedback from their ongoing interaction with external stakeholders including industry bodies, customers and suppliers, and the views of our shareholders through our ongoing investor engagement activities. The issues that we identified were placed into a matrix, and positioned for their level of importance to the Group and our businesses' stakeholders. We have identified the following issues as having the greatest potential impact on the Group:

Materiality matrix



Melrose Industries PLC Annual Report 2020

Commitment to playing our part

In conjunction with the development of our materiality assessment, we have reconfirmed our commitment to prioritising the pursuit of our four overarching sustainability principles, and aligned them with the UN SDGs and relevant underlying targets that apply to our business model, the businesses that we currently own, the sectors in which they operate, and their key stakeholders.

The integration of UN SDGs and their targets into our business model links our sustainability objectives with those of society and aligns our value creation strategy with our stakeholders.

Below, we have summarised our relevant UN SDGs, their respective targets, and examples of how we and our businesses are contributing to them.

Our Sustainability Principles	UN SDG	Our Sustainability improvement objectives	Our Key Sustainability actions	Further information
1 Respect and protect the environment	7 Affordable and clean energy 9 Industry, innovation and infrastructure 13 Climate action	• Invest in research and development to support and harness product innovation and quality within our businesses, to help their customers deliver on their commercial and environmental goals and to help find effective solutions to assist them in combatting climate change. • Drive divisional management teams to improve their operational, resource and energy efficiency to minimise the impact of their businesses' operations on the environment, including greenhouse gas (GHG) emissions and water usage. Improve Sell	• Melrose as a Group will achieve net zero GHG emissions by 2050. • Through 2021, we will develop a multi-year sustainability action plan to embed sustainable performance targets within our Group and business structure.	Environmental Leadership Pages 68 to 73
			• We will minimise the impact that we and our businesses' products have on the environment through innovative design and operational excellence. • We are committed to ensuring that our businesses achieve the highest standards of product quality, reliability and safety. • We will act ethically and with integrity and expect our suppliers to do the same. Where applicable, we have strict procedures in place to seek to identify whether 3TG (Tungsten, Tantalum, Tin, and Gold) minerals are sourced responsibly and from conflict-free regions of the world.	Sustainable and Safe Products Pages 62 to 67
2 Promote diversity and prioritise and nurture the wellbeing and skills development of employees and the communities that they are part of	3 Good health and well-being 5 Gender equality 8 Decent work and economic growth	• Drive our businesses to ensure the highest standards of health and safety for their people, as well as the protection of human rights, and encourage positive contributions to the communities in which they operate. • Implement effective policies and procedures, supported by local management accountability and a culture of strong awareness, training and investment in employees, to drive health and safety best practice. • Ensure the pension schemes that we inherit are managed prudently and effectively for both employees and retirees, and where relevant seek to create better-funded schemes with more prudent targets under our stewardship. • Promote inclusion and diversity at all levels. • Promote fair employment and skills development. • Ensure that our people have a voice and can inform executive decisions. Buy Improve Sell	• Stop all preventable accidents for employees and contractors. • Promote safe behaviours and monitor unsafe behaviours encouraging an enhanced focus on hazard identification and awareness.	Health and Safety Pages 74 to 77
			• We seek to create better-funded pension schemes with more prudent targets under our stewardship. • Melrose has achieved the 2021 Parker Review target of having one director from an ethnic minority on its Board. • Melrose is committed to achieving the Hampton-Alexander Review target in 2021 of having 33% female representation on its Board and has already achieved the Hampton-Alexander Review target of having at least 33% female representation within its Executive Committee and direct reports. • Melrose is committed to investing £10 million over five years through the Melrose Skills Fund in order to help build the UK's industrial base. • Our "Buy, Improve, Sell" business model improves financial performance, which in turn contributes to the economic development of the communities in which our businesses operate.	Our People Pages 78 to 85
3 Exercise robust governance, risk management and compliance	8 Decent work and economic growth	• Direct, oversee and challenge divisional management teams in implementing and enforcing effective compliance policies and business practices. • Ensure each division conducts business with integrity and in a responsible, ethical and sustainable manner. • Ensure the highest standards of product safety, and encourage our businesses to protect the ultimate wellbeing of their end-users by adhering to market standards and best practice. • Respect labour and human rights and support our businesses' suppliers to respect these principles throughout their supply chains. • Protect information security and data privacy. • Carry out prudent and responsible financial and tax planning and management and pay tax responsibly when due. • Maintain sensible and sustainable leverage to support investment. Improve Sell	• All employees, suppliers and contractors must comply with our Code of Ethics, conducting business with integrity and in a responsible, ethical and sustainable manner.	Ethics and Compliance Pages 86 to 87
4 Purposefully engage with key stakeholders to better understand and deliver on their expectations	8 Decent work and economic growth	• Engage where appropriate in regular, constructive dialogue with a variety of key stakeholders at each stage of our "Buy, Improve, Sell" cycle, and encourage and empower our businesses to do the same. • Maintain an informed focus on delivering improved returns for shareholders whilst also meeting best practice for sustainability performance, that is attuned to their expectations and concerns. Buy Improve Sell	• Melrose provides a consistent and transparent flow of information and management insight to shareholders and the wider investment community. • Melrose and its businesses regularly engage with employees across the Group, and enable key views of the workforce to be heard and considered by business unit executive teams where they can have the most impact. • Melrose has regular dialogue with various governmental and regulatory bodies regarding the undertakings and commitments given in connection with the acquisition of GKN.	Our stakeholders Page 61 Section 172 statement Pages 54 to 57

Our stakeholders

The success of our "Buy, Improve, Sell" model and our commitment to investing in our businesses to improve their sustainability performance relies on maintaining strong support from our key stakeholders, including our investors. Melrose provides a consistent and transparent flow of information and management insight to shareholders and the wider investment community, and we take an honest, transparent and open approach to investor relations and communications. We recognise that shareholders, as well as other stakeholders such as corporate governance agencies and independent reporting bodies, require robust information and guidance to best inform their decision-making. We deliver this through enhanced disclosure on topics that are material to the Company including sustainability, supported by active and transparent engagement, to enable our stakeholders to accurately review and assess our performance in line with best practice.

In addition to our annual programme of key information publications and engagement initiatives including the annual general meeting, general meetings on specific material items, publication of full and half year results, regular trading statements, and this Annual Report, the Board and the Melrose senior management team meet and communicate with shareholders on a frequent and proactive basis throughout the year, including at specific capital markets days on the different businesses we own.

Although the COVID-19 pandemic constrained our face-to-face activities in 2020 (and continues to do so), we continued to engage with our investors by providing trading updates, published more frequently during 2020 to ensure that investors were appropriately informed as to the Group's performance, and virtual capital markets presentation days to provide shareholders, analysts, and their representatives with direct access to the Directors and the opportunity to engage directly with the executive management teams of our largest businesses. Further information is available on the Investors section of our website.

Details about our stakeholder engagement during 2020, including our engagement with employees, suppliers and customers, and government bodies, can be found in our Section 172 statement on pages 54 to 57.

Melrose Industries PLC Annual Report 2020

Sustainable and Safe Products

UN SDG	Our Sustainability Principle	Our Key Sustainability actions
7 AFFORDABLE AND CLEAN ENERGY 9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 13 CLIMATE ACTION	Respect and protect the environment	We will minimise the impact that we and our businesses' products have on the environment through innovative design and operational excellence. We are committed to ensuring that our businesses achieve the highest standards of product quality, reliability and safety. We will act ethically and with integrity and expect our suppliers to do the same. Where applicable, we have strict procedures in place to seek to identify whether 3TG (Tungsten, Tantalum, Tin, and Gold) minerals are sourced responsibly and from conflict-free regions of the world.

Product responsibility is a core tenet of the Melrose model of acquiring and improving underperforming manufacturing businesses. This is grounded in safety and sustainable production practices, and demonstrated by sustainable product performance and effective product life cycle management. Examples of this include GKN Automotive's torque vectoring technology for all-wheel drive ("AWD") products that improves vehicle safety, and AQH's product development focus on improving the air quality inside the home by safely eliminating pollutants that can adversely impact human health. Furthermore, we recognise the risks and opportunities that the transition to a net zero emissions economy presents. Despite operating in some of the hardest industries to decarbonise, our businesses are well positioned to meet emerging regulatory requirements and wider environmental expectations. Through our significant investment, we help our businesses and their customers tackle pressing environmental challenges such as climate change.

Helping our customers address climate change

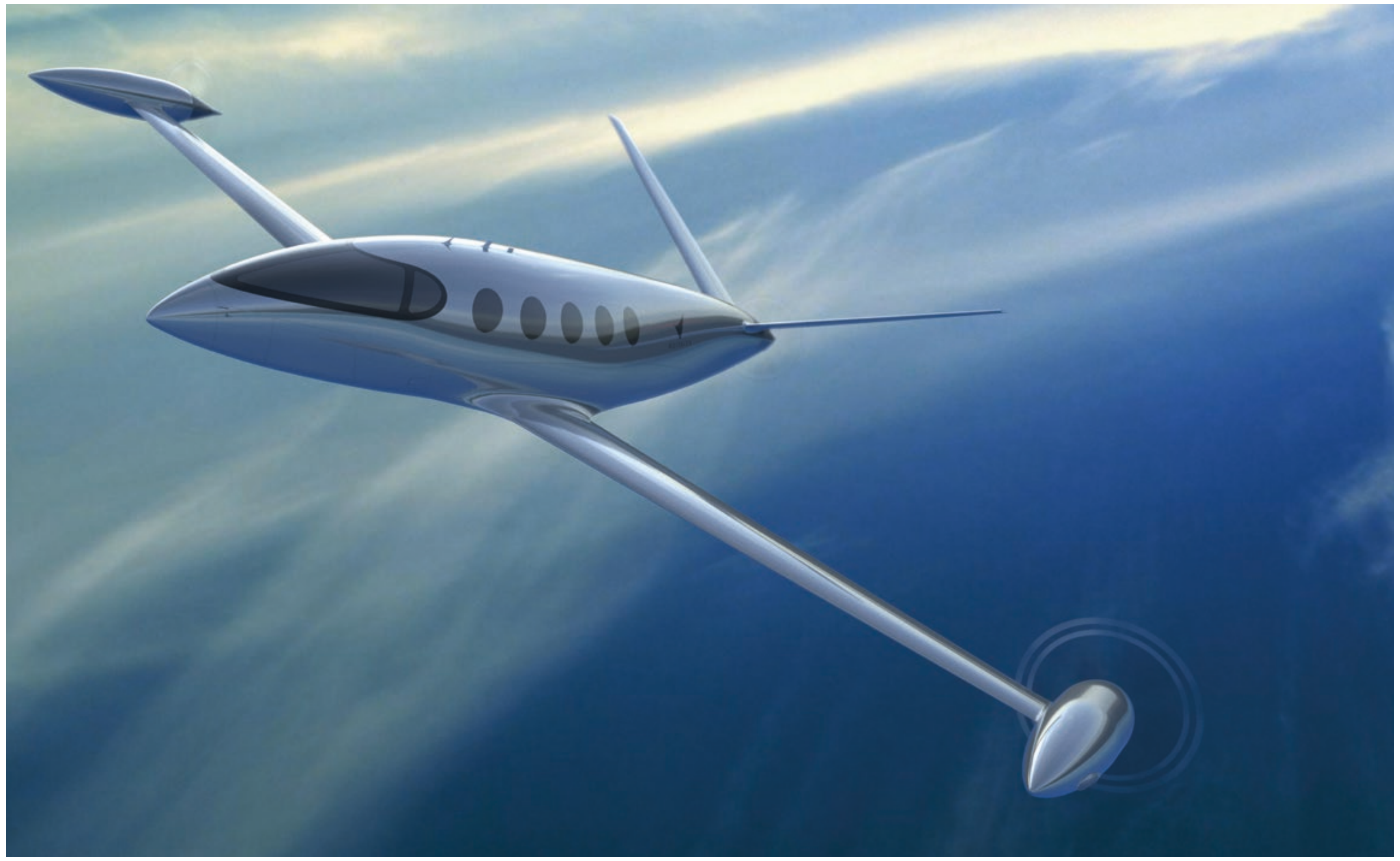
Cultivating the technical capabilities, innovation and foresight to provide effective solutions to the emerging sustainability challenges that our businesses' customers face is a key priority. We are taking active steps to anticipate how climate change will affect our businesses, and to drive positive climate action. We will continue to strengthen our understanding of the specific climate-related risks our businesses face, and work to mitigate these risks through alignment with the recommendations of the TCFD during 2021.

Climate-related issues have a direct impact on product strategy, development and financial planning across all of our businesses. Our businesses work closely with their customers and world-class research institutions to develop market-leading, cost-effective innovations, delivering solutions that address environmental challenges.

In 2020, our businesses invested over £150 million[1] in developing products that help their customers improve their energy efficiency and to reduce their GHG emissions, water consumption and waste generation compared with conventional technologies. More information on high profile projects including GKN Aerospace's investment and continued innovation in Additive Manufacturing to enable the development of their leading Fan Case Mount Ring structural design, GKN Automotive's cutting edge eDrive technology, and Nortek Air Management's StatePoint Technology® sustainable data cooling system, can be found within the Divisional reviews on pages 14 to 33.

> "We are committed to ensuring that our businesses achieve the highest standards of product quality, reliability and safety. In recognition of the importance of our businesses in protecting the wellbeing of the ultimate end-users of their products, each business follows strict product design and development procedures."

(1) Data has been collected from 95% (by R&D) of the Group.



GKN Aerospace continues to invest a significant proportion of its R&D spend each year[1] on enhancing fuel efficiency and reducing emissions within aircraft. The business leverages publicly available funding to support climate-related R&D, such as Clean Sky in Europe. Examples of recent and ongoing activities include:

- Signing the Joint Declaration of European Aviation Stakeholders related to Clean Aviation in Horizon Europe in June 2019, committing to a European Partnership towards achieving goals of the Paris Agreement. GKN Aerospace has committed to achieving net zero GHG emissions by 2050 and designing products that enable its customers to develop aircrafts that emit net zero GHG emissions throughout their life cycle by 2050. In order to meet these longer-term goals, GKN Aerospace has set an interim target of reducing its Scope 1 and Scope 2 GHG emissions by 5% annually.
- GKN Aerospace is a key partner in the Wing of Tomorrow composite spar project. The UK Aerospace Technology Institute funded programme led by Airbus UK aims to provide technologies for a sustainable Future Single Aisle Wing. A composite wing is the most significant opportunity for the Single Aisle airframe to improve aerodynamic performance, reducing global CO_2 emissions by many millions of tonnes every year. The work is being undertaken in GKN Aerospace's new Global Technology Centre in Bristol, UK, with the business investing more than £25 million in the programme over three years.
- GKN Aerospace is leading the development of a ground-breaking liquid hydrogen propulsion system for aircraft. The c.£55 million collaborative H2GEAR programme will push hydrogen technology and accelerate aerospace decarbonisation with the goal of zero CO_2 emissions hydrogen-powered sub-regional aircraft entering the skies as early as 2026. The H2GEAR programme will create more than 3,100 jobs across the UK and reinforces the UK's position at the forefront of aerospace technology research and development, as well as putting GKN Aerospace at the heart of the technology developments needed for the future of more sustainable aviation.
- Eviation and GKN Aerospace continue their quest to deliver the world's first electric commuter aircraft (Alice). In development since 2015, Alice will be capable of operating in the lower end of the regional market carrying nine passengers and two crew members on journeys up to 800km. Regional and domestic air travel account for a large part of aviation's CO_2 emissions, with CO_2 produced per km per passenger for flights of less than 500km almost double that of flights over 1,000km. Battery-powered aircraft are a key part of the journey towards zero-emission aviation. GKN Aerospace is providing its expertise across the integration of large-scale components including the complete wing, the complete tail including empennage, and electrical wiring interconnection systems. Design and manufacturing activities are already ongoing on-site at Eviation in Israel and in several GKN Aerospace engineering centres across Europe, and the companies are targeting an Entry into Service date of 2022.
- GKN Aerospace Sweden is leading in the testing of Sustainable Aviation Fuels. Groundbreaking development in the use of biofuels in aviation could lead to huge reductions in carbon emissions. Test flights using the Gripen RM12 engine powered 100% by biofuel have so far shown excellent performance both in flight and on the ground. The biofuel used is fully interchangeable with normal jet fuel and no engine changes or modifications are required.

(1) Gross budget for 2021 is c.£40 million.

GKN Powder Metallurgy's new e-pumps are substituting engine-driven pumps on vehicle transmissions.

A conventional automobile pump system causes the pump to be constantly driven, whether or not it is required, which causes energy wastage. The new e-pump system operates on demand, actuated from the electronic controlling unit of the car. This ground-breaking technology can achieve a fuel benefit of up to 10% compared to a conventional engine-driven pump operating within a conventional driving mode. For full hybrid and electric vehicles, the e-pump is the leading solution for lubrication and cooling.

In addition, see pages 24 and 25 for an overview of GKN Powder Metallurgy's Hy2Green hydrogen fuel storage technology.

GKN Automotive is at the forefront of increasing the efficiency of the products it manufactures.

At the GKN Automotive UK Innovation Centre in Abingdon, Oxfordshire, the business is helping progress the electric vehicle revolution and the ongoing decarbonisation of the global automotive sector. Projects based at the UK Innovation Centre include a partnership with the University of Nottingham and Drive System Design to develop the future generation of eDrive system platforms, including the world's lightest and most efficient electric vehicle powertrain suitable for the volume market, and Advanced Cooling and Control of High Speed e-Drive ("Ace Drive") technology, which targets: (i) a 25% reduction in packaging size and cost; (ii) a 20% drop in weight; and (iii) a 10% increase in efficiency compared to current equivalents, and production readiness by 2023.

As a result of the business's continued investment and focus in electric motors, GKN Automotive is now the market leader in highly efficient AWD systems, enabling its customers to improve fuel efficiency and reduce their carbon emissions. The Disconnect AWD technology provides around 80% more reductions in AWD-related CO_2 emissions than conventional AWDs. The new generation AWD components are 30% more efficient and 20% lighter than previous generations and are made from 98% recyclable materials. Product durability has been increased by 25%, and the use of expensive and supply constrained materials such as copper and rare earth elements has been reduced. These new products are more efficient, lighter (due to reduced material usage) and significantly longer lasting. The 510,000 systems of this type expected to be sold in 2021 will reduce vehicle emissions by more than 40,000 tonnes of CO_2 annually. In addition, the ePowertrain product line will invest approximately £70 million in 2021 in new products or in further enhancing existing products to support the CO_2 agenda.

Nortek Global HVAC through its Nortek Air Solutions division continues to develop best-in-class technologies that directly benefit communities around the world, and ensure continuity of critical infrastructure following a major weather or seismic event. Its air handling units rank 1, 2 and 3 in Miami-Dade County's High Velocity Hurricane Zone rating compliances for AHU cabinets. Earthquake-resistant climate control technology supplied to hospitals on the West Coast of the US have been proven to withstand a 6.7 magnitude seismic event for a duration of 30 seconds with virtually no damage.

Between 2018 and 2020, **AQH's** Broan division developed and introduced to market its AI Series Fresh Air System. Ever-increasing regulation to promote energy-efficient homes requires houses to be more airtight, which inherently creates a reduction in natural ventilation and can reduce air quality. The AI Series provides constant ventilation to homes to help improve indoor air quality, while reducing the energy impact. The system requires less energy to heat or cool a house and get the best air quality, and has an energy recovery rate of at least 75% of the previous energy cost.

In response to a growing need for a network of easily accessible and cost-effective electric vehicle charging points across the UK, **Brush** commenced a pilot project to develop and provide an integrated and containerised electric vehicle charging station solution. Through a combination of innovative design and technical excellence, Brush built a self-contained solution which could operate autonomously, be remotely monitored, and would require very little maintenance or intervention while also supporting the transition to a net zero carbon economy. The prototype solution, which comprises a 33kV Transformer, Switchgear, Vacutap® VBO tapchanger and condition monitoring, will be delivered by July 2021.

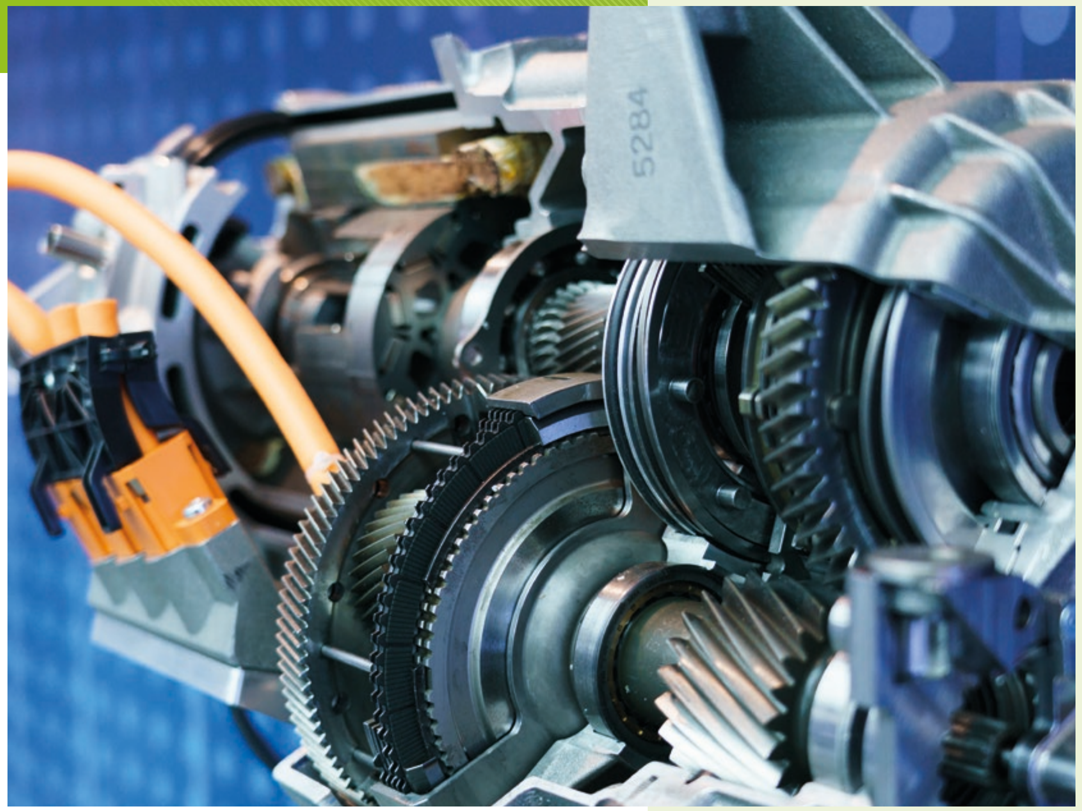
Ensuring the highest standards of product quality and safety

We are committed to ensuring that our businesses achieve the highest standards of product quality, reliability and safety. In recognition of the importance of our businesses in protecting the wellbeing of the ultimate end-users of their products, each business follows strict product design and development procedures to ensure precise delivery to customer specification, and to seek opportunities to enhance quality and safety performance.

The Group takes a preventative approach to product responsibility. We ensure that effective controls and processes are in place around social factors such as safety and quality assurance, including crisis management procedures and processes including, but not limited to, potential recall programmes.

In 2020, 92% of the Group's product portfolio (by revenue) was certified to a recognised international quality management standard of ISO 9001, ISO/IATF 16949 or EN/AS9100. All GKN Automotive and GKN Powder Metallurgy products are certified to the ISO/IATF 16949 standard, except for certain GKN Powder Metallurgy products which are certified to ISO 9001 (this standard is the application of ISO 9001 for automotive production and relevant service part organisations). Surveillance audits are conducted annually to ensure the standards are maintained, and re-certification occurs every three years. In addition, Nortek Global HVAC has committed to achieving ISO 9001 compliance across the entire organisation in 2021.

These high standards of product quality are recognised by our customers. GKN Aerospace has received more than 15 separate external recognition awards in the past three years, and its Hoogeveen and Papendrecht sites in the Netherlands have received the Boeing Silver Performance Award for three years in a row. Other customer awards received by GKN Aerospace have been from Lockheed Martin, Bombardier and Spirit AeroStructures.



Product life cycle management

Our businesses assess the impact of their products on the environment in terms of material usage, waste, energy usage and CO_2 emissions throughout each product life cycle. By incorporating circular economy principles in their design and manufacturing processes, our businesses can reduce their environmental impact and deliver products to their end markets with increased durability and longevity and reduced waste. Across the Group, life-cycle assessments have been completed for 11% of products (by revenue) with 10% of products (by revenue) certified to ISO 14040 and/or ISO 14044.

GKN Aerospace technologies ensure that only 20% of procured metal billets are removed in the production process, whereas the norm is up to 80%, therefore significantly reducing the 'buy to fly' ratio.

Nortek Global HVAC is aiming to reduce waste materials through better fabrication and manufacturing processes, with a cost saving target of US$20 million (£14.7 million).

To limit the end-of-life product impact on the environment, a number of our businesses are actively involved in product take-back programmes. **GKN Automotive** is involved in an initiative whereby old driveshafts are collected from designated garages and transformed into "as good as new" products with savings on energy, water, CO_2 and steel production. In addition, 100% of GKN Automotive's driveline products can be remanufactured for reuse.

GKN Powder Metallurgy performs life cycle product assessments certified with applicable standards (ISO 14040 and/or ISO 14044). The process is reviewed during third party external audits. Hazardous substances, GHG emissions, and raw materials are included in the review. Risks and opportunities are considered across all processes: design, development, procurement, production, transport, packaging, use, end-of-life treatment and end-of-life cycle. Several improvement actions have been identified following the completion of these assessments, including:

- recycling of metals and other materials to reduce landfill;
- conducting surveys on compressed air systems to reduce energy consumption from air leaks;
- eliminating or reducing the use of petroleum products; and
- improving manufacturing operations to improve energy efficiency and GHG emissions.

Designing products that require less materials whilst maintaining and improving performance is not only the right thing to do for the environment, but is commercially beneficial. **Brush's** Fusion software for design optimisation has resulted in up to 10% less materials and improved performance on its transformers. Brush has achieved an average reduction of 6% in copper, steel, polycarbonate and thermoplastics waste due to optimised manufacturing processes, and more optimised raw material, machined/pre-formed sections and extrusions.

Ergotron performs life cycle product assessments in accordance with the ANSI/BIFMA e3:2014 standard to reduce energy use, water use, and hazardous materials in production processes and end products. Life cycle assessments are performed on 100% of new office products and were completed on 21% (by revenue) of total products sold in 2020.

Our other businesses focus on reusability of products. All products made by **GKN Powder Metallurgy's** Hoeganaes division are 100% recyclable, and its powder is made from scrap. Furthermore, it takes back green (not yet sintered) scrap and unused powder from internal and external customers, re-mills it and mixes it back into new products.

The use of recyclable components is key to **AQH**, with its products being 90% recyclable based on their material composition.

Responsible sourcing

We are committed to ensuring that our businesses source raw materials and manufacture products in a responsible, ethical and sustainable manner. This applies to our businesses' global supply chains and is important in mitigating the risk of supply chain shocks.

We require our businesses to work closely with their suppliers to ensure they respect human rights and promote good working conditions across their supply bases. In practice, this means that suppliers are expected to treat their workers equally and with respect and dignity, for all workers to be of an appropriate age in compliance with the local legal minimum age for work, for all workers to be paid a fair wage that meets or exceeds the legal minimum standard or prevailing industry standard, to eliminate excessive working hours for all workers in compliance with local laws, and for all workers' health and safety rights to be protected at work.

Our businesses work with their suppliers to ensure that they conduct business in a manner that embraces sustainability and reduces environmental impact. We require our businesses to have strict procedures in place, in respect of sourcing products or raw materials containing 3TG minerals, to the extent required by applicable laws or customer expectations, to seek to identify whether 3TG minerals are sourced responsibly and from conflict-free regions of the world, as set out in the Group conflict minerals policy, which is available on our website. As a minimum, relevant suppliers are required to:

- perform due diligence to ascertain whether any 3TG minerals in products are conflict-free; and
- complete the Responsible Minerals Initiative reporting template or equivalent, as required by the respective business.

In line with our decentralised model, while the Board retains oversight of supplier-related Group policies that have applicability across the Group, such as the conflict minerals policy, responsibility for the implementation and management of all supplier-related policies rests with divisional management. The Group supports its businesses in implementing and managing such policies across their respective supply chains, in line with the nature and geographical representation of their supplier base.

Our businesses implement supplier qualification processes where relevant which, at a minimum, require suppliers to complete a risk assessment. Many of the businesses require suppliers to sign their supplier code of conduct or equivalent policies and depending on the determined level of risk, may also result in an audit or further reviews. GKN Aerospace, GKN Automotive and GKN Powder Metallurgy have each prepared a supplier code of conduct that applies globally to all their suppliers and is based on the ethos of "doing the right thing".

As well as providing high quality goods and services, our businesses are expected to operate in a manner that supports the Group's commitment to acting ethically and responsibly and is consistent with the Melrose Code of Ethics. Please see the Ethics and Compliance section on page 86 and 87 for more details.

Melrose Industries PLC Annual Report 2020

Environmental Leadership

UN SDG	Our Sustainability Principle	Our Key Sustainability actions
7 AFFORDABLE AND CLEAN ENERGY; 13 CLIMATE ACTION	Respect and protect the environment	Melrose as a Group will achieve net zero GHG emissions by 2050. Through 2021, we will develop a multi-year sustainability action plan to embed sustainable performance targets within our Group and the business structure. We will publish those targets.

Environmental performance in 2020

During 2020, operational energy consumption across the Group decreased by 14%, and between 2019 and 2020 our total Scope 1 and Scope 2 GHG emissions decreased by 11%. These significant reductions were achieved during a year that saw unprecedented lockdowns and associated working restrictions, which included temporary closures of certain of our businesses' production. Our businesses were proactive in preserving production capabilities during these times, and ensuring that employees could safely attend their sites at the earliest opportunity to mitigate preventable supply chain disruption.

Although it remains difficult to quantify the precise impact of COVID-19 restrictions on production, we recognise that temporary site closures were reasonably limited in duration, and in their impact on our businesses' operations. Most indirect production activities were maintained to preserve site integrity and allow our businesses the ability to ramp up production in response to customer requirements following the lifting of restrictions. With the full, longer-term impact of COVID-19 still under review across the world, we are pleased to have seen a strong improvement in the Group's emissions reductions outpacing the expected impact of COVID-19 disruption. This demonstrates our commitment towards driving sustainable production methods and infrastructure, and to minimising the potential negative impact that our businesses may have on the environment over the longer term.

Managing environmental performance

We are committed to ensuring that good environmental governance directly impacts the highest level of our businesses' executive decision-making, where it can have the most impact. In line with our decentralised model, our businesses are charged with identifying, monitoring and managing the environmental risks that affect their operating and market environments. Each business has frameworks in place for identifying principal risks and opportunities appropriate to that business, including climate-related risks. Each business's executive management team regularly reviews the significant climate-related issues, risks and opportunities related to their business. These reviews consider the level of climate-related risk that the business is prepared to take in pursuit of its business strategy and the effectiveness of management controls in place to mitigate climate-related risk. In 2020, each of the businesses carried out a climate change risk assessment, covering 88%[1] of the Group's operations in total. Any identified material risks are discussed with the Melrose senior management team and escalated to the Board where necessary.

With Melrose support, each business invests in and implements appropriate systems and processes to manage their impact on the environment, and continually reviews these in line with evolving best practices. At the end of 2020, 131 (81%) sites across our businesses were certified to ISO 14001 standard, and 26 sites (16%) had achieved ISO 50001 certification, in recognition of the businesses' strong focus on ensuring an efficient and sustainable use and management of energy.

Compliance to the standards is ensured by independent auditing. For example, in GKN Automotive, a full re-certification audit is carried out every three years for all sites by the external certification body SGS.

No material environmental fines or penalties were issued against any of the businesses in 2020 or in the previous four years.

We and our businesses strive to be open and transparent in our actions. In 2021, we will submit our environmental performance data to the CDP for the first time. This data will be publicly accessible through the CDP website at **www.cdp.net**.

(1) Data has been collected from 96% (by sites) of the Group.

Melrose's position on climate change

Improving operational efficiency is a key factor that shapes the long-term profitability and sustainability of our businesses and contributes to their compliance with increasing environmental standards and regulation. Our ambition is to achieve net zero GHG emissions in our Group's operations by 2050 in line with the UK Government's target, in order to achieve the goals of the Paris Agreement. As part of our evolving sustainability strategy, we aim to identify and implement relevant Group level targets to ensure we meet this goal.

The Group recognises the serious threat posed by climate change and the urgent need for meaningful action. We invest in and encourage our businesses to improve their operations and market offerings to minimise their impact on climate change and make them less vulnerable to climate-related risks, while safeguarding their long-term commercial success.

We are believers in industry, and in the potential of industry, to help solve society's most pressing needs. We buy high-quality but underperforming industrial businesses, with established positions in their markets.

Inherent in the nature of the manufacturing businesses that we acquire is that they often operate in the industries that are some of the hardest to decarbonise. By investing heavily in research and development, we enable our businesses to develop and provide the innovative and cost-effective solutions that their customers need to help tackle underlying causes of climate change.

Melrose sets a positive example and enables and empowers its businesses to follow its lead. Although the central Melrose carbon footprint is relatively limited, we offset the emissions that we generate. The Melrose corporate offices have attained the CarbonNeutral® company certification for 2019, 2020 and 2021 through a combination of internal energy efficiency initiatives and financing high-quality, high-impact emissions reduction projects in accordance with The CarbonNeutral Protocol[1]. The Melrose corporate office in the US has also achieved the HinesGo (Green Office) designation in recognition of its sustainability practices and energy efficiency performance, among other environmental and wellbeing criteria.

(1) Source: https://carbonneutral.com/the-carbonneutral-protocol.

Environmental reporting

This section of the report covers all entities over which the Group had financial control for a period of at least one year as at 31 December 2020. Emissions from entities acquired or disposed of during the reporting period (i.e. disposed of before 31 December 2020 or acquired on or after 1 January 2020) are not accounted for in this section.

Given that the Melrose business model is to buy, improve and sell businesses over a three to five-year time frame, the consolidated Group emissions data contained in this report can often show significant year-on-year changes, which may not reflect the underlying performance of each individual business in the Group.

In 2020, the Group achieved reductions in total energy and water consumption, waste generation, and Scope 1 and Scope 2 GHG emissions. The Group's activities were partially affected by the pandemic, which resulted in some temporary site closures.

However, as our businesses maintained the required site operations to ensure recommencement of production once restrictions were lifted, the reductions are not expected to be solely attributed to the pandemic as our businesses also continued to implement climate-related initiatives throughout 2020. It is hoped that these and future activities will support a long-term trend in energy and emissions reductions.

The Group's chosen intensity ratio is emissions reported above normalised tonnes, MWH, or m³ per £1,000 of turnover, which we believe remains the most appropriate intensity ratio for Melrose given our business model and structure. Although emissions decreased in 2020, total Group revenues decreased at a greater rate than emissions reduced, which caused an increase in the intensity ratios. This is a reflection of the prolonged reduction in demand due to the pandemic, while sites continued to operate.

This section has been prepared for the reporting period of 1 January 2020 to 31 December 2020, and in accordance with the principles and requirements of the Greenhouse Gas Protocol, Revised Edition, ISO 14064 Part 1 and the Environmental Reporting Guidelines, including the Streamlined Energy and Carbon Reporting guidance dated March 2020. The Greenhouse Gas Protocol standard covers the accounting and reporting of seven greenhouse gases covered by the Kyoto Protocol.

We have reported on all of the emission sources required under the Companies Act 2006 (Strategic Report and Directors' Reports) Regulations 2013 and under the UK's Streamlined Energy and Carbon Reporting (SECR) requirements. All material emissions from within the organisational and operational scope and boundaries of the Group are reported.

These sources fall within our consolidated financial statements. We do not have responsibility for any emission sources that are not included in our consolidated financial statements. We have used the GHG Protocol Corporate Accounting and Reporting Standard (revised edition), and data has been gathered in accordance with our GHG reporting procedure. The emission factors from the UK Government's GHG Conversion Factors for Company Reporting 2020 (DEFRA factors) have been used to calculate the GHG emission figures together with IEA country-specific factors for the associated overseas electricity usage.

Sustainability report
Continued

Greenhouse gas emissions

Table 1 shows the GHG emissions for the Group, broken down by Scope 1 and Scope 2 emissions.

Table 1: Total Melrose Group GHG emissions for the period 1 January 2020 – 31 December 2020 (tonnes CO_2e[1] unless stated):

	2020[2]	2019[3]	2018[4]	Change (2020/2019)[5]
Scope 1: Direct GHG emissions				
Combustion of fuel and operation of facilities[6]	184,874	223,847	23,261	-17%
Scope 2: Indirect GHG emissions				
UK electricity	17,614	26,909	1,718	-35%
Overseas electricity	711,898	774,569	29,592	-8%
Total purchased electricity	729,512	801,478	31,310	-9%
Other purchased energy	2,045	3,165	1,801	-35%
Total Scope 2[7]	731,557	804,643	33,111	-9%
Total Scope 1 and Scope 2 emissions	**916,431**	**1,028,490**	**56,372**	**-11%**
Company's chosen intensity measurement: Emissions reported above normalised tonnes per £1,000 turnover[8]	0.105	0.092	0.030	+14%

(1) CO_2e – carbon dioxide equivalent, this figure includes GHGs in addition to carbon dioxide, as set out in Table 2 below.
(2) The 2020 emissions data does not include GKN Wheels & Structures as it was sold part way through that year. The emissions from this business fall below our materiality threshold.
(3) The 2019 emissions data does not include the Walterscheid Powertrain Group as it was sold part way through that year.
(4) The 2018 emissions data does not include the GKN business units as they were acquired part way through that year.
(5) The percentage change is relative to the base year of 2019, the first full reporting year that GKN Aerospace, GKN Automotive and GKN Powder Metallurgy were part of the Group.
(6) Our Scope 1 figures include emissions from fuel used on premises, transport emissions from owned or controlled vehicles, losses of refrigerant, and process and fugitive emission.
(7) Our Scope 2 figures include emissions from electricity and heat purchased by the Group's businesses. Scope 2 emissions, and total GHG emissions, are calculated using the location-based method.
(8) The turnover figure used to calculate the intensity ratio does not include any share of revenues from entities in which the Group holds an interest of 50% or less.

For 2020 we have expanded our disclosure to describe the types of gases included within our Scope 1 and Scope 2 emissions disclosure provided in Table 1. Table 2 shows a breakdown of the Group's GHG emissions by type and by where those emissions were incurred. Our Scope 1 and Scope 2 emissions encompass methane (CH_4), nitrous oxide (N_2O), sulphur hexafluoride (SF_6) and tetrafluoroethane (R134a). The vast majority of our emissions are from carbon dioxide (CO_2), which is common among most industrial businesses. 2020 will be our base year for these calculations.

Table 2: Melrose Group GHG emissions by type (CO_2e) for the period 1 January 2020 – 31 December 2020 (tonnes CO_2e[1] unless stated)

	UK	Global (excl UK)	Total
Scope 1[1]			
CO_2	9,700	172,514	182,214
CH_4	13	227	240
N_2O	6	137	143
SF_6	2,075	741	2,816
R134a	0	59	59
Total Scope 1 CO_2e	**11,794**	**173,678**	**185,472**
Scope 2[2]			
CO_2	17,455	708,809	726,264
CH_4	54	466	520
N_2O	104	2,624	2,728
Total Scope 2 CO_2e	**17,613**	**711,899**	**729,512**

(1) Our Scope 1 figures include emissions from fuel used on premises, transport emissions from owned or controlled vehicles, losses of refrigerant, and process and fugitive emission.
(2) Our Scope 2 figures include emissions from electricity and heat purchased by the Group's businesses. Scope 2 emissions, and total GHG emissions, are calculated using the location-based method.

Table 3 shows the energy consumption by type for the Group, broken down by UK and overseas consumption, in accordance with the requirements of the SECR regulations. The Company's chosen intensity ratio in this regard is megawatts usage (MWh) per £1,000 of turnover. The scope of this disclosure has also been expanded for 2020 by including a more detailed breakdown of the various energy types.

Table 3: Melrose Group energy consumption by type for the period 1 January 2020 – 31 December 2020 (MWh unless stated)

	2020			2019			
	UK	Global (excl UK)	Total	UK	Global (excl UK)	Total	Change (Total)
Energy type	Energy (MWh)						
Natural gas	52,132	809,336	861,468	121,350	962,039	1,083,389	-20%
LPG	317	37,716	38,033	320	50,221	50,541	-25%
Gas oil	0	5,669	5,669	0	8,533	8,533	-34%
Fuel oil	0	9,189	9,189	0	21,538	21,538	-57%
Diesel	261	6,809	7,070	904	12,024	12,928	-45%
Petrol (gasoline)	13	667	680	39	2,177	2,216	-69%
Steam	0	21,713	21,713	0	30,253	30,253	-28%
Wood pellets	0	18,819	18,819	0	19,383	19,383	-3%
Total non-renewable fuels consumption	**52,723**	**909,918**	**962,641**	**122,613**	**1,106,168**	**1,228,781**	**-22%**
Total renewable electricity consumption	0	8,052	8,052	274	6,021	6,295	28%
Total non-renewable electricity consumption	75,549	1,864,732	1,940,281	108,459	2,055,094	2,163,553	-10%
Total electricity consumption	**75,549**	**1,872,784**	**1,948,333**	**108,733**	**2,061,115**	**2,169,848**	**-10%**
Total operational energy consumption	**128,272**	**2,782,702**	**2,910,974**	**231,346**	**3,167,283**	**3,398,629**	**-14%**
Company's chosen intensity measurement: MWh per £1,000 turnover[1]	0.015	0.318	0.332	0.021	0.283	0.304	9%

(1) The turnover figure used does not include any share of revenues from entities in which the Group holds an interest of 50% or less.

Environmental stewardship

As part of their improvement plans, our businesses seek to reduce their energy usage and GHG emissions within their operations through more efficient use of electricity, fuel and heat, by increasing the proportion of renewable energy where commercially viable, and by implementing other climate-positive actions such as sustainable transport initiatives for employees. The businesses take an appropriately tailored approach to implementing climate-related initiatives that are most relevant and impactful to improving their business activities and requirements, and their operational and market environments. Each business is at a different stage in their climate strategy depending on their maturity in this area.

Notable examples of climate-related initiatives and activities in 2020 include:

- **GKN Aerospace's** decision to move to full 'green' electricity use generated through renewable energy in the Netherlands, with an estimated saving of 12,200 metric tonnes of CO_2 annually from 2021. In addition, the Trollhättan site in Sweden, which consumes over 50 gigawatt hours (GWh) of electricity annually and is GKN Aerospace's largest site in Europe, began purchasing renewable energy from its local hydropower plant.
- Approximately 45,000 square metres of efficient LED lighting being installed at certain GKN Aerospace facilities in the US and Mexico, saving approximately 800,000 kWh per year in 2020.
- Continued promotion by GKN Aerospace (since 2017) of electric vehicle transportation for its employees. It has installed 26 dual point and 17 single point electric vehicle charging stations across eight of its facilities and shares five stations at a multi-tenant location for a total vehicle charging capacity of 74 vehicles per hour.
- **GKN Automotive's** European sites continue to drive energy efficiencies and cost savings with ongoing projects relating to LED lighting installation, improved building insulation, and investment in energy-efficient equipment including air conditioning and heating systems. Notable examples in 2020 include the installation of a roof top solar system at the Pune, India site with anticipated annual energy savings of 1,000,000 kWh, and at the Köping, Sweden site, where 100% of heating is now provided by district heating which is generated from industrial waste heat, waste incineration and biofuels.
- Investment in energy-efficient equipment by **GKN Powder Metallurgy**, with a strong focus given to replacing old and less efficient equipment with LED lighting, compressed air generators, motors and motor convertors.
- **Nortek Global HVAC** provides a bus system for employees to use to and from work at their sites in Mexico. This has eliminated more than 700 vehicle trips per day and their associated emissions.

In addition to the business-specific examples, the Group as a whole spent £304,579[1] on LED lighting retrofits in 2020.

(1) Data has been collected from 53% (by revenue) of the Group.

Water consumption

We encourage our businesses to reduce water consumption through implementing measures to lessen water use throughout the production process. Our businesses continue to make encouraging steps towards reducing their water use, including:

- **GKN Automotive** tracking water usage and waste generation as part of its product Life Cycle Assessment.
- **GKN Powder Metallurgy** is in the process of defining KPIs for water management performance along with annual improvement targets, as it recognises that water management performance is one of the business's key environmental challenges.

Water consumption data is presented in Table 4, showing a 7% decrease compared with 2019. We expect this was partially driven by temporary site shutdowns caused by the pandemic.

Waste management

Our businesses are actively encouraged to reduce the amount of waste they generate and to divert waste from landfill. An example of a business-specific initiative to reduce waste includes the continued expansion of **Nortek Global HVAC's** recycling programme, which has reduced the amount of waste sent to landfill by 25% from 4,530 tonnes in 2019 to 3,425 tonnes in 2020. Key recycling initiatives include its cardboard recycling programme with 1,200 tonnes recycled in 2020 (2019: 253 tonnes) and a new paper recycling programme with 11 tonnes recycled in 2020.

Table 5 shows the waste generation data for the Group in 2020, showing an overall decrease in the total waste generated, as well as the weight of both the non-hazardous and hazardous waste produced by the Group's businesses. Similar to the water consumption data reported below, we expect this was partially driven by temporary site shutdowns caused by the pandemic.

Table 4: Melrose Group water consumption data for the period 1 January 2020 – 31 December 2020[1]

	2020	2019	Change
Freshwater water consumption in operation (m^3)	3,880,393	4,165,220	-7%
Company's chosen intensity ratio: m^3 per £1,000 turnover[2]	0.443	0.380	17%

(1) Water consumption data was collected from 147 sites (93%) across the Group's businesses, up from 129 sites (80%) in 2019. Although a small number of sites did not record their water consumption, to give an indication as to size, these sites accounted for less than 3% of the Group's total GHG emissions in 2020, and so these omissions are not material.
(2) The turnover figure used does not include any share of revenues from entities in which the Group holds an interest of 50% or less.

Table 5: Melrose Group waste generation data for the period 1 January 2020 – 31 December 2020[1]

	2020	2019	Change
Weight of total non-hazardous waste (tonnes)	139,388	192,869	-28%
Weight of total hazardous waste (tonnes)	11,087	13,983	-21%
Total waste generated (tonnes)	150,475	206,852	-27%
Breakdown:			
- Total recycled (tonnes)	121,912	176,463	-31%
- Total incineration (tonnes)	9,103	-[2]	-
- Total landfill (tonnes)	15,601	8,248	+89%[3]
- Hazardous waste disposed through legally approved treatment routes (tonnes)[4]	3,859	-[2]	-

(1) Waste generation data was collected from 136 sites (86%) across the Group in 2020, up from 126 (78%) sites in 2019. Although a small number of sites did not record their waste generation, to give an indication as to size, these sites accounted for less than 3% of the Group's total GHG emissions in 2020, and so these omissions are not material.
(2) "Total incineration" and "Hazardous waste disposed through legally approved treatment routes" were reported for the first time in these categories in 2020 and therefore no prior year comparison is available. Hazardous waste was reported more generally in 2019, but for 2020 we have the data to provide a detailed breakdown as between the different categories of total waste generated, and feel this provides better disclosure.
(3) Total landfill for 2020 accounted for 10% of total waste generated, and the year-on-year increase was largely driven by a change in the sites included in the data coverage for 2020 compared to 2019. Some of the sites that reported for the first time in 2020 mainly send their waste to landfill, as well as some GKN Automotive sites showing an increase in landfill in 2020. We will look to achieve reductions in this area during 2021.
(4) This figure was calculated on the basis of the guidance published by the EU (see source: **https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:02000D0532-20150601**), which includes waste from physical and chemical processing of metals that are hazardous to humans and wildlife, oil spills and waste materials containing oil, wastes containing mercury and heavy metals, waste paint, varnish and coatings containing organic solvents and other hazardous substances.

Health and Safety

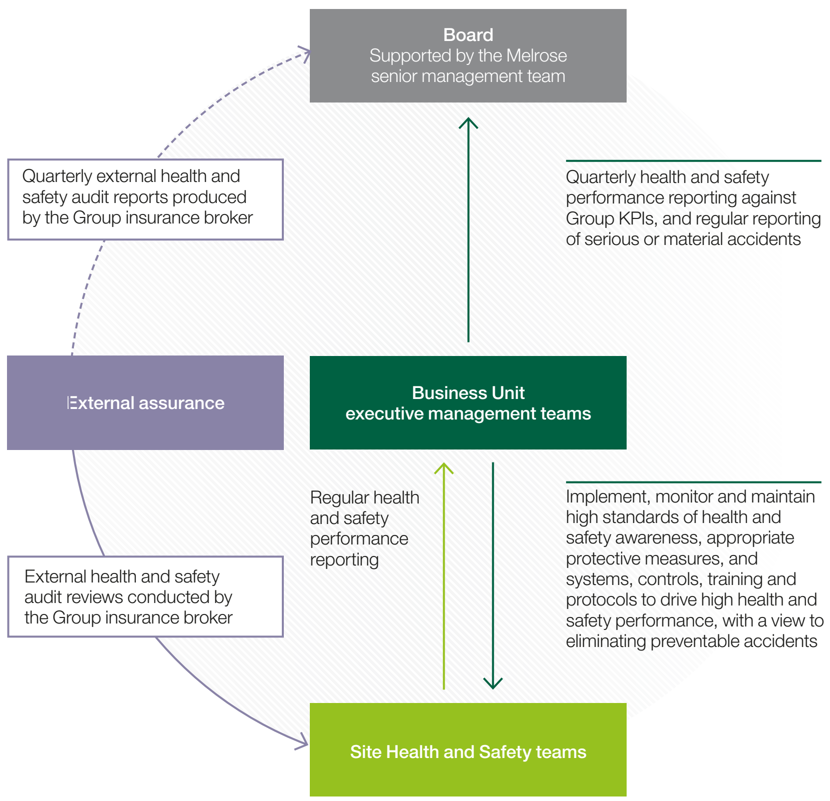
UN SDG	Our Sustainability Principle	Our Key Sustainability actions
3 GOOD HEALTH AND WELL-BEING	**Prioritise and nurture the wellbeing and skills development of employees and the communities that they are part of**	Stop all preventable accidents for employees and contractors. Promote safe behaviours and monitor unsafe behaviours encouraging an enhanced focus on hazard identification and awareness.

Safety first

We require our businesses to prioritise the health and safety of employees and contractors. We are committed to setting high standards and have effective policies, procedures and training in place to support the health, safety and wellbeing of all employees and contractors across the Group. We recognise the increasing importance of taking a holistic approach to employee wellness, to protect their physical and mental health and social wellbeing, and to foster a positive workplace culture that attracts and retains a highly skilled workforce. We are committed to ensuring that our employees are safe, and we drive our businesses to safeguard employee health and wellbeing across the Group.

The Group has a decentralised business model, employing 51,785 people globally (as at 31 December 2020) across Melrose and its eight businesses. In addition to the Group-level expectations for health and safety standards, each business is ultimately responsible for creating and maintaining their own safe and healthy workplaces, implementing operational best practices, and maintaining a robust culture of health and safety awareness, training and performance. This is delivered through the Group health and safety management framework.

Group Health and Safety Management Framework



> "We recognise the importance of taking a holistic approach to employee wellness, to protect their physical and mental health and social wellbeing, and to foster a positive workplace culture that attracts and retains a highly skilled workforce."

Health and safety management systems are implemented across all of our businesses to ensure that robust policies and procedures are in place to reduce risk and instil an enhanced focus on continuous improvement. Health and safety management systems are supported by internal health and safety effectiveness audits, external assurance reviews conducted by the Group's insurance brokers, with regular oversight and challenge by the Melrose senior management team.

As at 31 December 2020, 75%[1] of sites within the Group were certified to ISO 45001 or OHSAS 18001 (Occupational Health and Safety Assessment Series) international standards, with additional relevant sites progressing towards ISO accreditation. Across the GKN businesses, 100% of sites in GKN Automotive and GKN Powder Metallurgy, and 60% of sites in GKN Aerospace are certified to ISO 45001 or OHSAS 18001 standard. To maintain accreditation, third-party auditing is undertaken within a three-year certification cycle, with annual surveillance audits taking place in between to ensure standards are being maintained.

ISO 45001 was introduced in 2018 as the definitive global health and safety standard, replacing OHSAS 18001. A three-year migration period, due to end in March 2021, was extended to 11 September 2021 due to COVID-19. For those sites currently under the OHSAS 18001 standard, programmes are on track to migrate to ISO 45001 by September 2021.

(1) Data has been collected from 99% (by sites) of the Group.

Response to COVID-19

Melrose and its businesses took rapid and decisive action in response to the challenges posed by COVID-19. The many actions that were implemented across the businesses to keep our employees safe include the establishment of COVID-19 task forces and steering committees, which have been assigned responsibility for assessing and managing risks and ensuring clear communication to key stakeholders about the pandemic, and delivery of COVID-19 related safety training covering issues such as PPE, social distancing, and hand washing. Other measures included:

- global coordination of PPE, including supplies being shared across the businesses, and enhanced procurement of PPE to meet immediate and ongoing requirements;
- enhanced workplace cleaning and disinfecting protocols;
- working from home where duties could continue to be performed effectively;
- policies and procedures to assist in the identification of workers who had contracted the virus, to ensure they were instructed to stay at home;
- engineering and administrative protocols for social distancing;
- additional physical barriers introduced where necessary in factories and offices;
- increased provision of sanitising stations;
- regular PCR testing at high-risk sites; and
- return to work protocols, including management of processes to enable distancing and guidelines issued to employees on safe working.

Health and safety training

Employees across the Group's businesses received health and safety training in 2020.

89%

Health and safety training is a prerequisite to achieving our 'zero preventable accidents' goal, with all employees receiving training on a regular basis. Awareness of health and safety issues and the Group's policy on health and safety is included in induction training for all new joiners across the Group. 45,144(1) (89%) employees across the Group's businesses received health and safety training in 2020.

All employees within the GKN businesses have access to the online thinkSAFE! training portal and must complete at least one module per quarter. Over 90% compliance was seen in 2020, and the Group will continue to build on this and seek to increase this further. Training modules in 2020 included eight related to COVID-19 including coronavirus control measures, working from home fundamentals, and work-related stress.

Our businesses carry out technical health and safety training related to specific business activities. For example, **Nortek Global HVAC** provides training to staff on topics such as Control of Hazardous Substances, Chemical Exposure Control, Respiratory Protection, and Ergonomics.

(1) Data has been collected from 98% (by headcount) of the Group.

Case study

Nortek Global HVAC's "Accept Only Zero" initiative

The health and safety of our employees is a core strategic priority for the Group. Nortek Global HVAC has implemented an "Accept Only Zero" strategy with respect to health and safety incidents. In 2020, Nortek Global HVAC's proactive approach to safety resulted in 14,474 Behaviour Based Safety Observations (with feedback), 939 Site Leader Safety Gemba Walks, 6,897 Supervisor weekly inspections, 631 Near Misses reported, 1,108 Job Safety Analysis and Personal Protective Equipment assessments, and 1,454 LOTO/Machine Guarding assessments.

By focusing on leading indicators rather than the traditional lag indicators, the business has seen the number of injuries incurred at its sites decrease by 62% since 2018, and employees have become more engaged across all levels of the business in ensuring that health and safety best practices are adhered to.

Safety performance

We are focused on cultivating a strong safety culture within our businesses through emphasising the importance of preventing avoidable incidents and implementing near miss reporting, which encourages an enhanced focus on hazard identification and awareness. Behaviour-based programmes and continuous training and awareness campaigns remain central to the approach of all divisions in improving their safety performance.

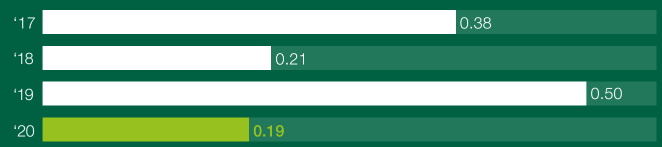
No fatalities were recorded across employees and contractors in the Group during 2020. To support the Group's overarching goal of stopping all preventable accidents for employees and contractors, the businesses have set enhanced targets for reducing injuries and occupational illness in the workplace, which include:

Business	Target	Areas of focus
GKN Aerospace	• Reduce lost time accident (LTA) rate by 10% per year. • Reduce total injury rate by 10% per year.	In 2021, four new health and safety awareness topics (one per quarter) will be added to the thinkSAFE! and thinkGREEN! online training portals, with a goal of achieving an attendance level 5 score, equivalent to over 91% completion by employees. The division's long-term goal is zero injuries.
GKN Automotive	• Reduce LTA rate by 20% per year.	GKN Automotive is focusing on reducing behavioural-related incidents and ensuring the right safety competencies are in place at all levels.
GKN Powder Metallurgy	• Reduce accident frequency rate by 10% per year. • Reduce accident severity rate by 10% per year. • Reduce serious injury rate by 10% per year.	GKN Powder Metallurgy has implemented a programme of internal audits, corrective action, and root cause elimination. There is a focus on prevention, rather than detection, which is delivered through a culture of performance monitoring.
AQH	• Reduce total recordable accident rate by 26% by 2023.	At site level, action-based goals are in place to drive hazard identification and employee engagement. In 2021, the business will implement a Safety Management System Evaluation that will provide a numerical score that correlates with a maturity rating. This data will enable AQH to set further quantitative targets in the future.
Ergotron	• Medium-term (2-5 years) goal to achieve zero injuries and occupational illnesses.	Ergotron has set ambitious goals across the short and medium term. The business is closely tracking near misses in order to proactively reduce safety incidents.

At a Group level, three key health and safety KPIs are measured. Weightings are applied to their respective reported health and safety performance according to the size of each business's workforce relative to the other businesses in the Group.

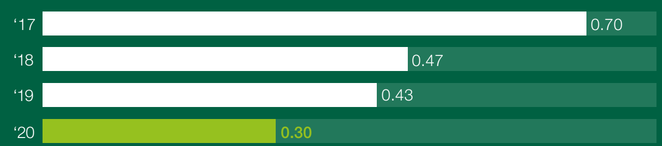
Major accident frequency rate

Records the average number of lost time accidents that have resulted in more than three days off work (defined as 'major' accidents), per 200,000 hours worked.



Accident frequency rate

Records the average number of lost time accidents, both major and minor, per 200,000 hours worked.



Accident severity rate

Records the average number of days an employee takes off work following an accident at work.

Employee wellbeing

The Group recognises the increasing importance of taking a holistic approach to employee wellness by protecting physical health, mental health and social wellbeing. This helps to foster a positive workplace, and to attract and retain a highly skilled workforce. In line with our wider Group health and safety framework, employee wellbeing programmes are implemented at a business level to ensure they are relevant to each business and most impactful. For example:

GKN Aerospace's Mental Health & Wellbeing Committee shares best practice in supporting employees with mental health and wellbeing initiatives in each region. GKN Aerospace has also produced a Think Health e-brochure, highlighting areas such as self-care and providing information on support resources available to employees.

GKN Automotive has introduced localised Employee Assistance Programmes which provide employees with access to counselling and support. There are a range of other health and wellbeing initiatives, including those focused on diet and lifestyle. For example, the GKN Automotive US healthcare scheme provides a discount to non-smokers to encourage smokers to quit, and support is also provided to enable them to do so.

Nortek Global HVAC offers a range of health and wellness benefits and support to its employees including access to an Employee Assistance Programme that provides counselling, mental health, financial and wellness support and a monthly wellness newsletter. Employees also benefit from discounted gym memberships.

Brush holds annual health and wellbeing days with the objective of raising awareness and promoting a healthy working environment with a view to enhancing productivity, individual performance and attendance.

Our People

UN SDG	Our Sustainability Principle	Our Key Sustainability actions
5 GENDER EQUALITY 8 DECENT WORK AND ECONOMIC GROWTH	Promote diversity and prioritise and nurture the wellbeing and skills development of employees and the communities that they are part of	We seek to create better-funded pension schemes with more prudent targets under our stewardship. Melrose has achieved the 2021 Parker Review target of having one director from an ethnic minority on its Board. Melrose is committed to achieving the Hampton-Alexander Review target in 2021 of having 33% female representation on its Board and has already achieved the Hampton-Alexander Review target of having at least 33% female representation within its Executive Committee and direct reports. Melrose is committed to investing £10 million over five years through the Melrose Skills Fund in order to help build the UK's industrial base. Our "Buy, Improve, Sell" business model improves financial performance, which in turn contributes to the economic development of the communities in which our businesses operate.

The Melrose Code of Ethics reinforces our sustainability principles, and provides employees with clear guidance as to how the Board expects them to conduct business, and the consequences of non-compliance. The Melrose Code of Ethics outlines the policies and procedures in place to drive best practice and to promote diversity and inclusion at all levels.

A great place to work

For our businesses to perform well and exceed their potential, it is important to nurture an engaged, capable and enthusiastic workforce. We want our people to enjoy the work they do, and to trust that their safety and wellbeing is our priority. We value and champion diversity in its broadest sense and drive our businesses to create working environments that encourage and nurture employees to grow, develop and act with integrity.

Employee engagement

We recognise the importance of engaging with our employees in a meaningful way in order to support their development and for us to deliver better business performance. We and our businesses regularly consult with employees across the Group, and this was particularly important in 2020 in light of the unprecedented disruption and uncertainty caused by the COVID-19 pandemic. Each of our businesses were highly responsive in addressing employee concerns, with increased direct communication between the businesses' executive teams and their wider workforces. For example, the CEO of GKN Automotive held live broadcast events for all employees across Europe, APAC and the Americas to discuss business performance and employee-related matters directly with the workforce. These events were recorded and uploaded to a newly created employee portal which also provided a source for executive team and local site-based messages.

Communication was increased with representative bodies, with GKN Aerospace increasing its contact with its works councils and other consultative bodies throughout the year. Other tailored methods of engagement were adopted by our smaller businesses. For example, Ergotron conducted a COVID-19 employee engagement survey to better understand productivity in the home workspace, engagement preferences, messaging around COVID-19 and overall wellbeing. Feedback from the survey was taken on board with the aim of improving employee wellbeing.

> "The workforce advisory panel played a key role in 2020 in allowing the businesses to share best policies and resources on how to engage with employees on COVID-19."

In 2019, Melrose established a Group workforce advisory panel ("WAP") to enable key views of the workforce to be heard and considered by our businesses' executive teams where they can have maximum impact. The WAP reports to the Board annually to provide visibility and oversight of key workforce views and also to ensure that the WAP and its underlying engagement processes are operating effectively for each business.

The WAP is chaired by a member of the Melrose Executive Committee and comprises the Chief Human Resources Officer (or equivalent) from each business. Each member of the WAP is responsible for promoting workforce engagement, disseminating information, collating the voice of their workforce through workforce engagement and demonstrating how that voice is fed into executive management decisions. The WAP played a key role in 2020 in allowing the businesses to share best practices and resources on how to engage with employees on COVID-19 and to prepare them for returning to work where national lockdowns had been enforced and then lifted. The feedback received from the WAP is discussed at Board meetings along with the whistleblowing report (see page 86 for further details on the Group whistleblowing policy).

Melrose requires all of its businesses to safeguard the contractual and statutory employment rights of their respective employees. Each business is also encouraged to maintain constructive relationships with employee representative bodies, including unions and works councils. We respect the rights of workers across all businesses to participate in collective bargaining and freedom of association. Workers, without distinction, have the right to join or form trade unions of their own choosing and to bargain collectively in relation to a host of employee related matters. Workers' representatives are not discriminated against and have access to carry out their representative functions in the workplace. In 2020, 20,539[1] (40%) of our employees belonged to a recognised trade union (2019: 34%; 2018: 31%; 2017: 29%; 2016: 31%).

Group employees as at 31 December 2020

Permanent full-time employees	49,668
Temporary employees	1,389
Apprentices	728[2]
Total	**51,785**

(1) Data was collected from 99% (by headcount) of the Group in 2016, 99% (by headcount) in 2017, 71% (by headcount) in 2018, 69% (by headcount) in 2019 and 99% (by headcount) in 2020.
(2) Data was collected from 93% (by headcount) of the Group.

Reward and recognition

Our businesses have policies in place on recruitment, talent development and succession planning, supported by training programmes and effective management. Opportunities exist across all the businesses for employees to discuss career development with their direct managers, and each business encourages internal applications for open positions. In 2020, 25% of open positions were filled by internal candidates[1].

	2020	2019	2018	2017
Open positions filled by internal candidates	25%	31%	15%	20%
Overall voluntary attrition	10%	10%	25%	21%

Performance evaluations are undertaken across our businesses, with 49%[2] of employees having received a performance appraisal in 2019 (2018: 51%). At the time of this report, performance evaluations for 2020 were ongoing. Annual salary reviews are aligned with performance evaluations to ensure employees are paid fairly and correctly for the position they hold. In compliance with all applicable local laws relating to the provision of pensions, 44,878 (87%) of the Group's employees benefit from being a member of a company-based pension scheme. Other forms of workplace recognition are also in place. For example, GKN Aerospace hosts annual excellence awards, with awards given to employees who have contributed to decision-making and the direction of the business at a divisional and/or site level.

In Focus

Pensions

With every acquisition, Melrose seeks to strengthen pension scheme arrangements for the benefit of employees and retirees. Since its establishment in 2003, Melrose has contributed £704 million to the pension schemes of its businesses. We take pride in having substantially improved all the UK pension schemes under our ownership, with many of them becoming fully funded on departure from the Group. For example, under Melrose ownership the McKechnie UK pension scheme was improved from 58% funded at acquisition to more than fully funded upon leaving the Group, and the FKI UK pension scheme was improved from 87% to fully funded upon its departure from the Group. Both of those schemes were sold into Honeywell International Inc., a US-listed group with the financial covenant strength expected of a market capitalisation exceeding $140bn. For further details, please refer to page 6.

Our focus on strengthening pension schemes begins from when we acquire a new business, and the GKN pension schemes are the latest example of this. The GKN UK defined benefit pension schemes had been chronically underfunded and we were proactive, transparent and constructive in agreeing commitments with pension trustees during the acquisition of GKN. Prior to acquiring GKN, we committed to providing up to £1 billion of funding contributions, doubling annual contributions to £60 million, and providing £150 million of upfront contributions. In our short period of ownership, we have met our commitments and have significantly strengthened the pension schemes and cut the accounting deficit on the GKN UK defined benefit pension schemes by over 80% since just before acquisition.

Our model for ensuring the long-term prosperity of our businesses' pensions schemes is founded on the following principles:

- Improve funding targets to ensure improved financial health for the long-term sustainability of our businesses' pension schemes.
- Increase funding levels to begin an enhanced level of immediate support during our period of stewardship.
- Provide better structural and financial security to our businesses' pension schemes during our ownership.
- Insist on independent chairs to govern our businesses' pension schemes in accordance with governance best practice.

Securing our employees' and retirees' futures through responsible stewardship of their pensions is of strategic importance to the Board.

For further information on Melrose's engagement with pension scheme trustees and our investment in transforming the UK defined benefit pension schemes of our businesses, please refer to page 5.

(1) Data was collected from 82% (by headcount) of the Group in 2017, 96% (by headcount) in 2018, 66% (by headcount) in 2019 and 66% (by headcount) in 2020.
(2) Data was collected from 96% (by headcount) of the Group in 2018 and 97% (by headcount) in 2019.

Diversity and inclusion

We prioritise creating and maintaining a diverse, inclusive and safe environment within our businesses. We recognise the importance of diversity in building a high-calibre workforce, and we are committed to championing diversity in the broadest sense, be that along geographical, cultural or personal lines, encompassing gender, race, ethnicity, country of origin, nationality, colour, social and cultural background, religion, family responsibilities (including pregnancy), sexual orientation, age and disability. We are actively engaged in finding ways to increase diversity across the Group, and the sectors in which our businesses operate.

Melrose ensures that entry into, and progression within, the Group is based on aptitude and the ability to meet set, fair criteria outlined in job descriptions. For any employees with a disability, we take steps to ensure reasonable adjustments are made where required. Melrose is proud to be a member of the Business Disability Forum, a not-for-profit member organisation that works with the business community to understand the changes required in the workplace for disabled persons to be treated fairly, so that they can contribute on an equal-opportunity basis to business success, to society and to economic growth.

The Melrose Code of Ethics highlights the importance of diversity and inclusion and is supported by our diversity policy, which is reviewed and approved each year by our Nomination Committee. Copies of these policies can be found on our website at **www.melroseplc.net**. Further details on diversity can also be found in our Nomination Committee report on pages 108 to 109. The Nomination Committee has ultimate oversight and responsibility for ensuring the diversity policy is adhered to and the individual business executive management teams are responsible for ensuring day-to-day compliance with the diversity policy.

Promoting diversity at all levels

Melrose leads its businesses by example, starting at Board level. The Board requests diverse candidates within shortlists, and two of the most important roles on the Board, being the Senior Independent Director and the Chairman of the Audit Committee, are held by a woman. Further, 100% of Director appointments in the past three years have been women[1].

As at 31 December 2020, Melrose had 30% female representation on its Board. Melrose had been on track to achieve the Hampton-Alexander Review target of having 33% female representation on its Board by the end of 2020 with the intended retirement of Mr David Roper in May 2020.

However, as a result of the global pandemic, the Board and Nomination Committee agreed that it was not the appropriate time to lose the expertise and experience of one of its co-founders. The Board's decision to delay Mr Roper's retirement was the reason that Melrose did not achieve its goal of 33% female Board members by the end of last year as intended. Melrose is committed to achieving the Hampton-Alexander Review target in 2021, and in anticipation of Mr Roper's retirement, it has started the process of recruiting for a new female Non-executive Director.

Gender diversity within the Melrose Group Board

	At 31 December 2020		At 31 December 2019	
	Male	Female	Male	Female
Board[1]	7 (70%)	3 (30%)	7 (70%)	3 (30%)

(1) Mr Peter Dilnot joined the Board on 1 January 2021, bringing total number of Board members to 11. Mr Roper will retire from the Board in May 2021 having delayed his retirement by 12 months due to COVID-19.

Melrose also recognises other forms of diversity and has achieved the Parker Review target of having one Director from an ethnic minority background on the Board by the end of 2021 following the appointment of Ms Funmi Adegoke to the Board in October 2019.

Diversity is valued below Board level. The Melrose Executive Committee, having been established in 2020, consists of 35% female representation, exceeding the Hampton-Alexander Review target of 33% female representation within executive teams and their direct reports.

Whilst recognising that the Melrose "Buy, Improve, Sell" strategy means that we inherit the shape of our workforces, our businesses are encouraged to promote diversity once they have entered the Melrose Group. GKN Aerospace has external partnerships to help promote diversity with OUTstanding (a network which commends LGBT+ executives and allies who are not only successful in their own careers but also in creating supportive workplaces for other LGBT+ people), and Where Women Work (an organisation which celebrates women's achievements in the workplace while recognising the companies that support them).

GKN Aerospace has continued implementing the 'Inspired Women's Leadership Development Programme' with the professional training and coaching organisation 'Forward Ladies', designed to help women in the organisation succeed and to encourage women to mentor other female colleagues in the business. Furthermore, the Black Lives Matter movement, and in particular the George Floyd protests, accelerated Ergotron's planned implementation of its updated Equality, Diversity and Inclusion (EDI) Programme and EDI all-employee survey. This was accelerated following feedback from employees to have further education in this area.

Through the Melrose Skills Fund, Melrose is working on a project to help improve socio-economic and ethnic diversity within the engineering sector as a whole. This project is being led by Enginuity, a not-for-profit organisation that leads on several initiatives to support the engineering and manufacturing sectors, and also involves input from Unite the Union. The project is in the early stages of development and will involve creating an engineering task-orientated computer game contextualised for the aerospace sector with a focus on sustainable projects. This will be piloted in targeted schools in order to attract young people to the engineering industry who may not normally apply. The game will provide further resources on working in the engineering sector, including the skills and qualifications that are needed to apply, and further information on potential work experience opportunities. Melrose is also looking to work with Enginuity on a project to help upskill older Group employees. This project will be developed further in 2021.

Gender pay gap reporting

The gender pay gap indicates the percentage difference in the mean and median base and bonus pay between all men and women in the workforce. Gender pay gap reporting legislation in the UK requires employers with 250 or more employees to publish information every year indicating the pay gap between their male and female employees. This legislation is currently applicable to four companies within the Group, including GKN Aerospace Services Limited, which chose to voluntarily report in 2020 on its 2019 data despite the reporting requirements having been suspended due to COVID-19.

GKN Aerospace Services Limited saw its trend in median gender pay gap markedly improve in 2019, having reported a median gender pay gap of 14.7% (2018: 16.4%). Its gender pay gap was materially smaller than the UK's national average median gender pay gap (17.4%) and the company also achieved a significantly smaller median gender pay gap than the industry average for manufacturing companies (18.1%)[(1)].

All of our Group companies that are required to report on their 2020 data will do so by the October 2021 deadline.

Senior managers

Melrose is required to report on gender diversity at a senior manager level. In accordance with section 414C of the Companies Act 2006, the definition of senior managers is required to include Group employees who are directors of Group undertakings but excludes the Board of Melrose Industries PLC. Melrose does not consider that including the employee directors of its undertakings provides an accurate reflection of the senior management at Melrose, nor its executive pipeline. As reflected in note 3 to the financial statements, Melrose has many undertakings, including dormant, non-trading and immaterial subsidiaries that we have inherited and do not remain in the Group for long. We have 35% female representation on our Executive Committee which represents a more accurate reflection of the senior management team and executive pipeline at Melrose. Melrose has increased female representation among its senior managers under section 414C by 4 percentage points since 2019.

Total Group employee gender diversity at 31 December 2020

	Male	Female	Total	Male (%)	Female (%)
Total Group employees	**41,405**	**10,380**	**51,785**	**80%**	**20%**

Senior Managers diversity at 31 December 2020

Senior managers (section 414C of the Companies Act 2006)	Male	Female	Total	Male (%)	Female (%)
Employees in senior management positions	19	8	27	70%	30%
Directors of group undertakings, excluding the above	149	19	168	89%	11%
Total Senior Managers	**168**	**27**	**195**	**86%**	**14%**

(1) Source: Office for National Statistics Gender Pay Gap Tables 1.12 and 16.12.

Talent and career management

Skills development

Melrose champions talent development and recognises the importance of investing in human capital. Our businesses are proactive in anticipating both short and long-term employment needs and skills requirements for the long-term success of their business. This is central to Melrose's strategy to boost productivity and improve business performance. Extensive training opportunities are available and promoted to all workers at all stages of their careers to ensure that high skills levels are cultivated and maintained across the Group.

We are committed to promoting employee career development and life-long learning. Training programmes across the businesses start with new-hire onboarding programmes to accelerate knowledge and exposure to the business's culture and objectives.

All employees are encouraged to actively engage in their career development and a wide range of learning opportunities are available throughout their career, extending beyond functional skills development to personal development and leadership opportunities.

Training and development

	2020	2019	2018	2017	2016
Average training time per employee (hours)[(1)]	13	15	3	9	-
Average training spend per employee (£)[(2)]	166	222	128	142	152
Total number of training hours[(3)]	**338,406**	**410,638**	**39,823**	**37,951**	-
Total annual spend on workforce training (£)[(4)]	**8,591,293**	**12,182,473**	**1,200,461**	**1,377,247**	**300,025**

(1) Data was collected from 38% (by headcount) of the Group in 2017, 21% (by headcount) in 2018, 25% (by headcount) in 2019 and 39% (by headcount) in 2020. Data was not available in 2016.
(2) Data has been collected from 99% (estimate of spend as only AQH Zephyr Pacific location and Melrose head office not included) of the Group.
(3) Data was collected from 38% (by headcount) of the Group in 2017, 21% (by headcount) in 2018, 25% (by headcount) in 2019 and 39% (by headcount) in 2020. Data was not available in 2016.
(4) Data has been collected from 99% (estimate of spend as only AQH Zephyr Pacific location and Melrose head office not included) of the Group.

Leadership training is an integral part of ensuring the workforce remains engaged and innovative, whilst enabling the businesses to develop a diverse pipeline of successors for key roles and leadership positions. The businesses have developed their own leadership programmes that are most relevant to their employees and organisations. However, there are elements that are consistent across all businesses.

Annual talent reviews and regular check-ins between managers and employees identify individuals who have the ability and aspiration to grow into more stretching roles. Leadership training programmes are in place for high performing employees to support their transition from individual contributor to first leadership position and beyond. The programmes are becoming increasingly popular and have received positive feedback. GKN Aerospace has identified 174 people as potential future participants in their leadership programme. Since 2019, 45 people have participated in the Future Leaders programme and since June 2018, 77 people have taken part in the Leaders of Leaders programme. Furthermore, 64 employees at GKN Automotive have completed leadership programmes over the last year.

GKN Aerospace launched its Lean Learning Academy in 2020, with the curriculum designed to provide frameworks to improve performance and reduce inefficiencies using the Lean Six Sigma principles. In 2020, 853 people were trained, and 698 achieved certification on Lean capabilities. In 2021, the plan is to certify over 3,000 people at Lean Foundation level, over 750 people at the Lean Advanced level, over 500 at the Six Sigma Green Belt level and 50 at the Six Sigma Black Belt level.

In-person training programmes were largely put on hold in 2020 due to COVID-19, which caused a decline in both overall training hours and spend on training. Online training was adapted to focus on supporting the remote workforce, with modules such as 'leading remote teams' and 'driving collaboration remotely' introduced in a number of businesses. We expect our businesses to build on their flexible delivery programmes to improve their training engagement levels in 2021.

Apprenticeships and graduate programmes

Apprenticeship programmes assist with training a new generation of employees and help to ensure that knowledge is retained within the businesses. In 2020, 728[1] apprenticeships were in place across the Group's businesses, of which 96% were within the GKN Aerospace, GKN Automotive and GKN Powder Metallurgy divisions.

GKN Aerospace sits on the Aerospace Trailblazer Apprenticeship Employer Group to help shape future apprenticeships and is also an employer partner for the West of England Institute of Technology, which focuses on advanced engineering and high value manufacturing. GKN Aerospace's Filton and Western Approach schools' engagement team have been working on activities to recruit more female apprentices over the last four years. As a result, within the GKN Aerospace Bristol apprenticeship programme, 17% of the overall apprentice population is now female. In recognition of their strong commitment and continuous improvement of their apprenticeship programmes, GKN Aerospace's Filton and Western Approach UK sites were named 'Large Employer of the Year' for the sixth consecutive year, and one of its apprentices was awarded 'Outstanding Apprentice of the Year' in each case in the 2020 Bristol & Bath Apprenticeship Awards.

We also place a strong focus on training and developing graduates, with some of the Group's largest businesses including GKN Aerospace, GKN Automotive and GKN Powder Metallurgy each running global graduate programmes. In September 2019, GKN Aerospace launched its graduate programme with the first cohort meeting in January 2020 for their first development week. The programme will continue to support global graduates in 2021 through its structured development framework, preparing some graduates to move into leadership or technical roles. GKN Aerospace plans for its third global cohort to start in September 2021.

Apprenticeship and graduate programmes across the GKN Aerospace, GKN Automotive and Brush businesses are supported by the Melrose Skills fund, which was launched in 2019.

(1) Data has been collected from 92% (by headcount) of the Group.

In Focus

Melrose Skills Fund

The Melrose Skills Fund was launched in 2019 to provide the financing to develop the capabilities required to build the UK's industrial base, and is utilised by our GKN Aerospace, GKN Automotive and Brush businesses. With a commitment to invest £10 million over five years through the creation of STEM programmes, apprenticeships and degrees to invest in manufacturing hubs, digital skills, and employee development, Melrose is helping to equip the UK with the future skills it needs to grow its industrial skillset.

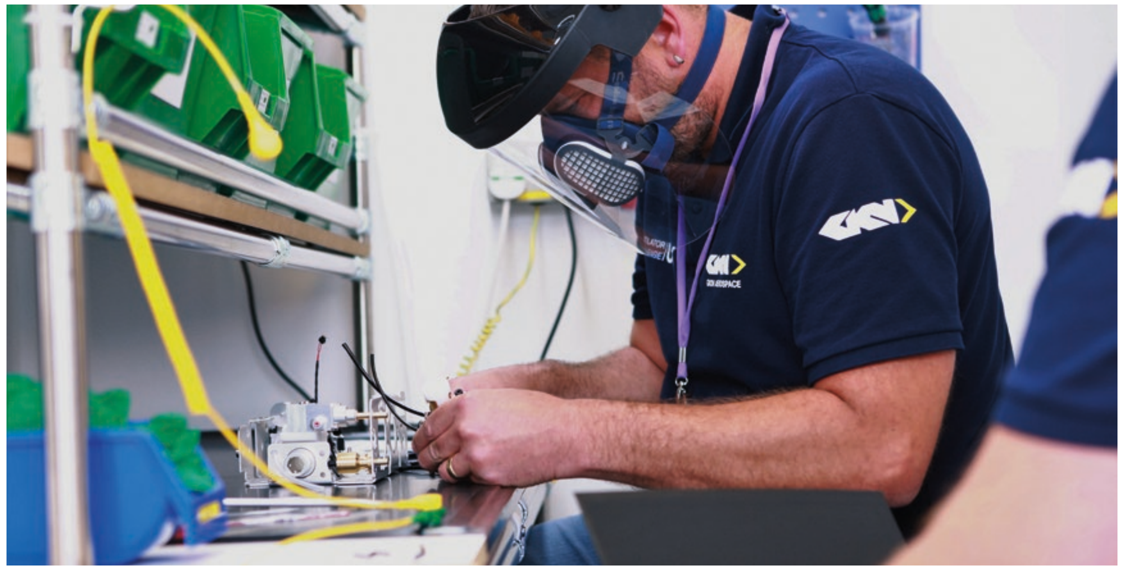
In 2020, GKN Aerospace developed and delivered new training and digital learning modules to upskill its teams. Foundation topics for digital learning modules such as Introduction to Jet Engines, Aircraft Familiarisation, Geometric Dimensioning and Tolerancing received excellent feedback from the user community. Almost £200,000 was invested on a range of training programmes which have so far been completed by more than 300 people. The Global Technology Centre in Filton has established a Learning and Education Hub where future training programmes will be hosted and active engagement with early careers (schools and colleges) will be pursued. A number of exciting projects are lined up for 2021 to continue to build new skills and capabilities in line with new technologies such as electrification and alternative fuels, and effective use of digital technologies to improve efficiency and add value to our customers.

GKN Automotive has also continued to utilise the Melrose Skills Fund to support its UK Innovation Centre in Abingdon, Oxfordshire, which focuses on developing skills and R&D capability. In 2020, the Skills Development Programme at Abingdon saw two apprentices complete their L3 apprenticeship, one apprentice graduate to an L6 Levy-Funded degree, and four degree students complete their "ABI Year-in-Industry" assignment. A number of internal staff are also undertaking qualifications at the Innovation Centre. In addition to qualifications, the Innovation Centre has supported several other skills development initiatives, including working with local secondary schools on STEM events, and delivering training to nearly 100 external individuals to deliver the VentilatorChallengeUK (detailed further on page 85).

In 2020, Brush utilised the Melrose Skills Fund to enhance internal capabilities and support skills development across a range of topics including leadership skills, project management essentials, and environmental impact assessment training. The business also supported a range of student internships from 12-month placements to summer programmes.

Melrose is also working on a diversity project which is supported by the Melrose Skills Fund with the aim of increasing socio-economic and ethnic diversity within the engineering sector. This project is being led by Enginuity and involves Unite the Union. Further details can be found on page 82.

Community partnerships



Our businesses promote the social wellbeing of employees by encouraging them to actively contribute to local charitable and community projects, and lead by example through the sponsorship of such projects. The Group made cash donations to not-for-profit charitable organisations[1] in 2020 of £634,221 (2019: £799,196; 2018: £312,485). The Group made cash expenditure to community projects[2] in 2020 of £532,613 (2019: £229,038, 2018: £113,441).

- **GKN Aerospace** and **GKN Automotive** were at the heart of the VentilatorChallengeUK consortium of manufacturing companies making desperately needed medical ventilators for NHS hospitals, enabling staff to care for patients worst affected by COVID-19. Employees worked around the clock at no profit to the business and the relevant teams delivered more than 13,000 ventilators, an incredible 12 years' worth of normal production in 14 weeks.
- **Melrose** is a proud sponsor of the work being conducted at Newcastle University on the Human Cell Atlas project. The aim of this project is to create a comprehensive reference map of all human cells for a better understanding of human health and diagnosing, monitoring and treating disease.
- **GKN Powder Metallurgy** supports an extensive list of local charitable causes and community projects, with employees encouraged to volunteer their time and expertise. In 2020, the company contributed around £180,000 through cash donations and community spend.
- In August 2020, **Nortek Global HVAC** launched the 'Nortek Gives' community service initiative, which encourages each employee to live out its mission statement of Creating a Better Tomorrow Every Day by providing one community service day each year for each employee to give back to the communities in which they live, work and play. As an example, project engineers from the Montreal, Canada site led a virtual engineering workshop to encourage high school students to pursue a career in the field. Students were tasked with building beehives to help increase the presence of wild bees near the crops they pollinate. As would be the case in a commercial engineering project, students were guided on how to overcome financial and technical constraints.

(1) Data was collected for 84% (by administration expenses) of the Group in 2018, 64% (by administration expenses) in 2019 and 62% (by administration expenses) in 2020.
(2) Data was collected for 73% (by administration expenses) of the Group in 2018, 65% (by administration expenses) in 2019 and 100% (by administration expenses) in 2020.

In Focus

Filter for Life

Our businesses are focused on giving back to their local communities and providing volunteer opportunities for employees. A great example of this is Nortek Global HVAC's partnership through its Nortek Air Solutions division with the charitable organisation Center of Family Love (CFL).

Nortek Air Solutions provides career opportunities to more than 130 adults with physical and intellectual disabilities through the Filter for Life (FFL) centre in Kingfisher, Oklahoma. Residents who work at the FFL facility hand make air filters in a variety of custom sizes. The programme gives residents an opportunity to develop and grow their skillset while making a positive impact on their community. Nortek Air Solutions has donated equipment, and employees have assisted in projects to improve workflow and efficiency at the FFL facility.

Employees have also volunteered in other areas of CFL's campus. This has included providing mentoring to residents, cleaning up debris after a storm, and designing a visiting booth to allow residents to safely visit family during the COVID-19 pandemic.

Ethics and compliance

UN SDG	Our Sustainability Principle	Our Key Sustainability actions
8 DECENT WORK AND ECONOMIC GROWTH	Exercise robust governance, risk management, and compliance	All employees, suppliers and contractors must comply with our Code of Ethics, conducting business with integrity and in a responsible, ethical and sustainable manner.

Exercise robust governance, risk management, and compliance

Sound business ethics and integrity are core to the Group's values and are fundamental for the success of our strategy. Melrose is a UK premium listed company with strong, established financial controls that are continually assessed, tested and reviewed. This robust framework is supported by an independent internal audit function, regular public disclosure and financial reporting, external audits, public accountability and conformance with leading benchmarks set by the UK Corporate Governance Code. It is also supported by investor requests and direct engagement with them and corporate governance and proxy advisors, and extensive engagement with the Group's wider stakeholder base to ensure best market practice is implemented.

The high standards of financial and non-financial controls, and strong governance backed by internal and external auditing of financial and non-financial compliance, are enforced throughout the Group. Directors, officers, employees, and contractors throughout the Group, whether permanent or temporary, and in respect of any entities over which Melrose has effective control, must comply with Melrose's Code of Ethics, which was updated in 2020 to reflect current best practice and strong corporate citizenship. Each business is required to communicate and embed the Code of Ethics within their operations and activities to ensure that they conduct business with integrity and in a responsible, ethical and sustainable manner.

The Code of Ethics, which can be found on our website (**https://www.melroseplc.net/about-us/governance/code-of-ethics/**), has been approved by the Board and includes policies covering best practice with respect to anti-bribery and corruption, anti-money laundering, anti-facilitation of tax evasion, competition, conflict minerals, trade compliance, data privacy, whistleblowing, treasury and financial controls, anti-slavery and human trafficking, document retention, and joint ventures.

Implementation is supported by risk assessments, audits and reviews and annual compliance certifications. Melrose strongly believes that policies and procedures are only as effective as the people who implement them. To that end, all of the above measures are backed by investment, resources and training.

The Audit Committee reports directly to the Board. It oversees the Group's internal control processes and, together with the Board, monitors breaches of the Melrose Code of Ethics. Please refer to pages 44 to 45 for full details on the Group's approach to risk management.

Anti-bribery and corruption

We take a zero-tolerance approach to bribery, corruption and other unethical or illegal practices, and are committed to acting professionally, fairly and with integrity in all business dealings and relationships, within all jurisdictions in which we and our businesses operate. Melrose requires its businesses to adopt high governance standards, to ensure that the Group conducts business responsibly, sustainably, and in the pursuit of long-term success for the collective benefit of stakeholders. This is outlined in our anti-bribery and corruption policy, which is implemented and administered throughout the Group.

Melrose prohibits lobbying involvement and political involvement of any kind across the Group.

Whistleblowing

Melrose runs a Group-wide whistleblowing platform, which is overseen by the Audit Committee reporting to the Board and supported by the Melrose senior management team. The platform is monitored by the businesses' legal, compliance and HR functions, with support from the Melrose senior management team. All employees have access to a multi-lingual online portal to raise concerns, confidentially and anonymously, about possible wrong-doing in any aspect of their business, including financial and non-financial matters. The businesses undertake a number of measures to bring awareness to employees of the whistleblowing platform, using online and offline media as appropriate. Employees who come forward with a genuine concern are treated with respect and dignity and do not face retaliation. During 2020, 128 whistleblowing cases were recorded. This highlights the effectiveness of awareness campaigns together with the trust placed by employees in the whistleblowing programme. Each case is investigated confidentially by the business with appropriate response measures taken. Whistleblowing cases are regularly reported to the Audit Committee and ultimately, to the Board.

Modern slavery and human trafficking

As set out in the Melrose anti-slavery and human trafficking policy, the Group has a zero-tolerance approach to any form of modern slavery. In accordance with the Modern Slavery Act 2015, Melrose publishes its own Modern Slavery statement, which is approved by the Board annually and can be found on our website (**https://www.melroseplc.net/media/2568/modern-slavery-statement-june-2020.pdf**). Under Melrose's decentralised group structure, each business is responsible (where applicable) for publishing their own Modern Slavery Statement in accordance with the requirements under the Modern Slavery Act 2015, with support provided by Melrose where needed. This approach ensures that those senior managers closest to the business operations devise appropriate measures to eradicate slavery from their supply chains.

Melrose drives its businesses to implement employee training with respect to anti-slavery and human trafficking, to ensure that employees understand the risks and are prepared to take the required action if they suspect that modern slavery is happening internally or within the supply chain.

Human rights

We are committed to acting in an ethical manner with integrity and transparency in all business dealings, and to create effective systems and controls across the Group to safeguard against adverse human rights impacts. The Group has a strong culture of ethics and integrity and works to ensure adherence to the Melrose Code of Ethics, which encompasses key human rights considerations. The Group supports the principles set out in the UN Declaration of Human Rights.

Our businesses also implement effective and proportionate measures to identify, assess and mitigate potential labour and human rights abuses across their operations or supply chain. These include training, modern slavery policies, employee handbooks and business-specific policies. All business-specific employee policies are reviewed locally within each business in order to ensure compliance with local laws and standards as a minimum. As at 31 December 2020, 99%[(1)] of direct (tier 1) suppliers had been assessed against labour and human rights standards.

There have been no violations reported on human rights by our Group businesses in 2020 and for the previous two years.

Paying tax responsibly

Melrose is committed to paying taxes that are due, complying with all applicable laws, and engaging with all applicable tax authorities in an open and cooperative manner. The Group does not engage in aggressive tax planning. The Group's Tax Strategy is reviewed, discussed and approved by the Board annually. The Audit Committee periodically reviews the Group's tax affairs and risks.

The Group has adopted a policy in respect of the prevention of the facilitation of tax evasion which has been implemented by the businesses, with guidance on undertaking risk assessments and training to employees in relevant roles.

The Group does not reside in countries considered as partially compliant or non-compliant according to the OECD tax transparency report, or in any countries blacklisted or grey listed by the EU, for the purposes of tax avoidance and/or harmful tax practices, per the latest lists released as at 31 December 2020.

(1) Data coverage of the Group is 93% (by Cost of Sales).

Protecting information security and data privacy

Melrose strongly respects privacy and seeks to minimise the amount of personal data that it collects, as well as ensuring the robust and sufficiently segregated storage of any data that is held. Information security and cyber threats are an increasing priority across all industries globally, and like many businesses, Melrose recognises that the Group must be protected from potential exposures in this area, particularly in light of its scale, reach, complexity and public-facing nature, as well as the potential sensitivity of data held in relation to civil aerospace technology and controlled defence contracts.

The Melrose senior management team continues to work with the divisional executive teams and external security consultants to track the Group's exposure to cyber security risk and, to ensure appropriate compliance with the GDPR, mitigation measures are in place for the Group.

Melrose has deployed its information security strategy and risk-based governance framework to all businesses within the Group, which follows the UK Government's recommendations on cyber security. This strategy has enabled risk profiling and mitigation plans to be developed for each business to mitigate and reduce their exposure to cyber risk in a manner that is adequate for their level of sophistication. This ensures clarity and consistency in the assessment of IT and cybersecurity matters across our diverse and decentralised Group. The progress of each business is measured against the information security strategy and is monitored on a quarterly basis.

The Board supported by the Melrose senior management team oversees the Group's cyber security risk profile and, in line with our decentralised model, each business is required to protect their business and personal information, ensuring safe and appropriate usage of their IT systems and processes by their employees.

To mitigate the impact of external cyber-attacks, the Melrose senior management team works with the executive teams of each business and external security consultants to review each business's cyber risk profile to monitor and drive continuous improvement actions. The results of this ongoing review programme are reported to the Board on a quarterly basis.

Through a hosted, externally auditable self-assessment process, each business is reviewed and reports on their compliance in key areas of cyber management incorporating disaster recovery processes and business continuity plans, cyber incident response plans, applications and database management including access controls testing, appropriate security products, policies and procedures, confirmation of appropriate change management processes for all business-critical systems, IT inventory listings including all classified data to meet compliance with legal and regulatory requirements, monitoring and logging of all cyber incidents, physical environment access controls and network security, regular security training, and management of third party access control.

The businesses regularly perform internal and external testing of their perimeter defences through penetration testing, ensuring appropriate threat monitoring systems are in place. All of our businesses follow and work towards national and international business accreditations in varying aspects of cyber management where applicable and relevant to their business activities, including the UK's National Cyber Security Strategy (NCSS), ISO 27001, and industry-specific NIST in the defence sector and TISAX in the automotive sector.

As part of Melrose's overall information security strategy, IT Security awareness training was deployed by all businesses in 2020.

Looking forward to 2021

We made strong progress during 2020 in embedding our key sustainability principles throughout the Group, mapping the material sustainability issues that matter most to the Group's business activities and our key stakeholders, and aligning the Group's activities with Melrose's overarching sustainability ambitions and relevant UN SDGs. We look forward to accelerating that progress during 2021 by augmenting our sustainability improvement initiatives and ongoing reporting, continuing to actively promote and invest in the decarbonisation of the industries that our businesses operate in, protecting our workforce, upholding strong ethical and governance principles and practices, and building innovative products that enable us, our customers, and our key stakeholders to achieve the transition to a net zero carbon economy.

The Strategic Report, as set out on pages 1 to 87 has been approved by the Board.

On behalf of the Board

Simon A Peckham

Simon Peckham
Chief Executive
4 March 2021

Melrose Industries PLC Annual Report 2020

The Board is committed to maintaining the high standards of corporate governance required to ensure that the Company can continue to deliver on its strategic goals, and to achieve long-term success for the benefit of its stakeholders.

Justin Dowley
Non-executive Chairman

As part of this approach, the Board has applied the principles and complied with the provisions of corporate governance contained in the UK Corporate Governance Code (the "Code") issued by the Financial Reporting Council (the "FRC") and available to view on the FRC's website at: www.frc.org.uk.

In support of this commitment, the Board carried out a number of key governance activities during 2020 designed to ensure that Melrose remains compliant with the provisions of the Code and to enable continuous improvement in line with best practice corporate governance guidelines.

Impact of COVID-19

As is described elsewhere in this Annual Report, 2020 was undoubtedly defined by widespread disruption to production and trading environments caused by the COVID-19 pandemic. In times of crisis, it is even more critical that high standards of corporate governance are maintained by the Board. In addition to its scheduled quarterly meetings, the Board held weekly meetings during the initial height of the pandemic to ensure close oversight of critical issues across the Group, backed up by weekly cash management meetings held with the divisional executive teams driven by site level bottom-up financial information to enhance the focus on cash generation, analyse trading, cash and working capital, and implemented measures to reduce cost and accelerate working capital efficiency improvements. We also felt it was important to publish more frequent trading updates to ensure that investors were appropriately informed as to the Group's performance and the impact of the pandemic on the Group, supported by regular bespoke interactions between investors, analysts, and members of Melrose senior management. The Board will continue with some elements of this reinforced governance structure in 2021 as the effects of the pandemic continue to be felt.

Succession planning

Succession planning continued to be an area of focus for Melrose in 2020. The Nomination Committee and the Board considered the leadership needs of the Group, present and future, together with the skills, experience and diversity needed from its Directors going forward. We recognise that succession planning is an ongoing process and is critical to maintaining an effective and high-quality Board.

During the year, Executive Vice-Chairman Mr David Roper had intended on retiring from the Board. However, as a result of the global pandemic, the Board and the Nomination Committee agreed that it was not the appropriate time to lose the expertise and experience of one of its co-founders. Mr Roper therefore agreed to delay his retirement to assist the Company in navigating its way through the challenges presented by the pandemic. Mr Roper will instead retire on 31 May 2021. His knowledge and experience have been very helpful in ensuring that the Group ended the year in a strong position. We thank him for his long and successful service, particularly for the last twelve months, and wish him all the best.

As a result of the valuable contribution that Mr Peter Dilnot has made since joining Melrose as Chief Operating Officer in 2019, the Board in consultation with the Nomination Committee approved the appointment of Mr Dilnot to the role of executive Director, and such appointment took effect on 1 January 2021. We welcome Mr Dilnot to the Board.

Succession planning arrangements by the Board as a whole were reviewed in 2020. This included reviewing the skills set, tenure, diversity and independence of those already on the Board in order to ensure that the right balance of skills, experience and diversity were reflected and being developed. Following such review, the Nomination Committee recommended to the Board that a new female Non-executive Director should be appointed. Stonehaven International has been retained to recruit for this role. Further details are outlined in the Nomination Committee report on page 108.

Melrose Executive Committee

The Melrose Executive Committee operates under the direction of the Chief Executive. It is chaired by a member of the Melrose senior management team on a rotating basis to encourage diversity, and comprises members of the Melrose head office team from London, Birmingham and Atlanta. The Melrose Executive Committee meets on a weekly basis and executive and Non-executive Directors attend by invitation. Its key roles are to ensure that there is full knowledge of, and coordination between, the Melrose central team on all important issues, to consider what, if any, actions are required that week in respect of acquisitions, disposals and day-to-day management, to ensure that the appropriate resource is being devoted to resolve any such issues, and to ensure that actions being taken are supportive of the Group's aims, objectives and culture.

Remuneration

The Directors' Remuneration report, comprising the annual statement from the Chairman of the Remuneration Committee and the Annual Report on Remuneration, is available on pages 110 to 126.

Following a successful consultation with shareholders earlier in the year, the current Directors' remuneration policy was approved at the 2020 AGM and was effective from the close of that meeting. The Directors' remuneration policy was subsequently amended with effect from the close of the general meeting that took place on 21 January 2021 to incorporate the 2020 Employee Share Plan (see below).

As further detailed in the Directors' Remuneration report, the decision to renew the Company's management incentive plan arrangements was postponed given the sudden impact of COVID-19 in March 2020. Following an extensive and detailed follow-on consultation with key shareholders and proxy advisors later in the year, a proposal to renew the arrangements was made to shareholders in December 2020, with the 2020 Employee Share Plan (and consequent changes to the Directors' remuneration policy) being strongly approved by shareholders in January 2021.

Melrose's remuneration philosophy remains unchanged in order to align senior management with shareholders: executive remuneration should be simple, transparent, support the delivery of the Melrose value creation strategy and pay only for performance.

COVID-19 response

2020 was undoubtedly defined by widespread disruption to production and trading environments caused by the COVID-19 pandemic. This included a sharp market decline in the aerospace sector due to unprecedented global travel restrictions. Each of the Group's businesses and their respective production and market geographies were impacted by the COVID-19 pandemic to various extents, with the most common effects across the Group being the temporary reduction of manufacturing capacity and reduced requirements due to lockdown measures and international travel restrictions.

We and our businesses implemented strong and responsive measures during 2020 to mitigate the impact of COVID-19, primarily centred around enhanced cash management, minimising operational disruption, and above all else, protecting the health and safety of the Group's workforce. Actions included:

- Publishing trading updates more frequently to ensure that investors were appropriately informed as to the Group's performance and the impact of the COVID-19 pandemic and the economic environment on the Group. This was supported by frequent bespoke interactions between investors, analysts, and members of management.
- Weekly meetings of the Board to ensure close oversight of critical issues across the Group.
- Holding weekly cash management meetings with the divisional executive teams driven by site level bottom-up financial information to: enhance the focus on cash generation; analyse trading, cash, and working capital; and implement measures to reduce cost, accelerate working capital efficiency improvements, and preserve cash until market conditions improve.
- Close and regular monitoring of order books, cash performance, cost control and other leading indicators at a Group level to guide our businesses in mitigating the impact of adverse trading conditions.
- Global coordination of PPE supplies and distribution across the Group to enable our smaller businesses to benefit from the scale and influence of our larger businesses.
- Board and senior management took a reduction in salary to mirror the difficulties faced within the Group, and the wider economic disruption.
- Contingency planning for potential future lockdowns and the implementation of strong protective measures, including the building of short-term inventory buffers for 2021.
- Revising production processes and operations to ensure employees could return to work safely, based on wide, regular, and direct consultation with the workforce.
- Increased flexible working options to enable the workforce to work from home, supported by increased engagement with the workforce via remote means, to discuss business performance and employee-related matters.
- The Group's largest businesses were at the heart of the VentilatorChallengeUK consortium providing round the clock resources at no profit in the national effort to deliver more than 13,000 ventilators in approximately 14 weeks.

We thank our shareholders for their continued support of our management team and business model; our employees for their extraordinary efforts; and our supportive banking syndicate, who have ensured that the Group had access to finance throughout 2020 including temporary covenant relief to provide the Group with the flexibility, if required, over the medium term, to continue to improve our businesses, despite the periods of unprecedented market turmoil that were experienced due to the global pandemic.

For further detail about these and the other significant and accelerated actions that we and our businesses took to minimise the impact of COVID-19 during 2020, please refer to the following sections:

Finance Director's review	pages 36 to 42
Risks and uncertainties	pages 46 to 53
Corporate Governance report	pages 97 to 102
Section 172 statement	pages 54 to 57
Sustainability report	pages 58 to 87
Audit Committee report	pages 103 to 107

Melrose Industries PLC Annual Report 2020

Governance overview

Sustainability

The Board is mindful of its responsibilities regarding sustainability and has carefully considered how it can deal with matters relating to sustainability in the most efficient and appropriate way, in light of Melrose's decentralised model and the industries in which its businesses operate. The Board oversees and retains ultimate responsibility for Melrose's initiatives, disclosure and reporting in respect of improving the sustainability performance of its businesses. The Board receives external training annually and quarterly updates on key sustainability issues that impact the sectors within which the Group's businesses operate, and on the specific measures that are required to be implemented to drive improved sustainability performance over the longer term for the benefit of all stakeholders.

Risk management and compliance

Melrose has implemented a uniform Enterprise Risk Management programme across all its business units. Our processes and procedures are now fully embedded in all Group businesses.

Our Code of Ethics (which can be found at **https://www.melroseplc.net/about-us/governance/code-of-ethics/**) reinforces our values and provides guidance for all employees, contractors and business associates so that they are fully aware of what is expected of them, their responsibilities and the consequences of non-compliance. All business units are required to ensure that the Code of Ethics is communicated and embedded into their business operations. Each business unit is also required to ensure there is a mechanism in place for anyone to whom the Code of Ethics applies to seek guidance on interpreting its principles, where required. This is supported by a compliance framework comprising policies covering best practice with respect to anti-bribery and anti-corruption, anti-money laundering, anti-facilitation of tax evasion, competition, conflict minerals, trade compliance, data privacy, whistleblowing, treasury and financial controls, anti-slavery and human trafficking, document retention and joint ventures.

In 2020, the Melrose Code of Ethics and Group compliance policies were updated to bring them up to date for key regulatory and legal developments and to align them more closely with the Group's sustainability principles. The policies have been implemented across all business units together with refreshed risk assessment guidance, and continue to be monitored to ensure their effectiveness for the Group. The Group also introduced its first Group-wide conflict minerals policy, and further details about this can be found on page 67 of this Annual Report. Taken together, these initiatives have enhanced our businesses' effectiveness at identifying and managing risks and have promoted and embedded a more risk-aware culture. Further details on the Group's management of risk can be found on pages 44 to 45 of this Annual Report.

Melrose's reputation for acting responsibly plays a critical role in its success as a business and its ability to generate shareholder value. We maintain high standards of ethical conduct and take a zero-tolerance approach to bribery, corruption, modern slavery and human trafficking and any other unethical or illegal practices. We are committed to acting professionally, fairly and with integrity in all business dealings and relationships, within all jurisdictions in which we operate. Further details of the Group's stance and focus on ensuring effective stewardship in respect of key environmental, social and governance matters are set out in the Sustainability report on pages 58 to 87. Supporting our updated compliance policies are a comprehensive online training platform, an industry-leading whistleblowing reporting facility and a data-driven risk reporting dashboard providing increased risk management visibility and trend analysis to senior management and the Audit Committee. The integrity of the compliance framework is further reinforced by the use of independent assurance and compliance audits.

Main responsibilities of the Board

- Effectively manage and control the Company via a formal schedule of matters reserved for its decision.
- Define the Group's purpose, determine and review Group strategy and policy to deliver that purpose, and provide strategic leadership to the Group.
- Set the Group's values and behaviours that shape its culture and the way it conducts business.
- Consider acquisitions, disposals and requests for major capital expenditure.
- Review financial and trading performance in line with the Group's strategic objectives.
- Ensure that adequate funding and personnel are in place.
- Engage with stakeholders and key shareholders on issues that are most important to the long-term success of the Company.
- Oversee the effective operations of the workforce advisory panel in ensuring the views of the Group's business unit workforces are considered in its discussions and decision-making.
- Report to shareholders and give consideration to all other significant financial matters.
- Agree Board succession plans and consider the evaluation of the Board's performance over the preceding year.
- Oversee the Group's risk management and internal control systems.
- Determine the nature and extent of the risks the Group is willing to take.
- Agree the Group's governance framework and approve Group governance policies.
- Monitor, assess and review cyber security and fraud risk for the Group.
- Delegate and oversee responsibility for entrepreneurial leadership and strategic management of the Group to the Group senior executives.
- Challenge, review and exercise robust managerial oversight across key decisions, actions and processes performed by the Group's business units.
- Promote the success of the Company over the long term for the benefit of shareholders as a whole, having regard to a range of other key stakeholders and interests.
- Oversee and retain ultimate responsibility for Melrose's enhanced sustainability initiatives, disclosure and reporting in respect of improving the sustainability performance of its businesses.

Engagement with stakeholders

Engagement with key shareholders and governance bodies continued throughout 2020 on a number of important topics including diversity, sustainability and remuneration.

In advance of the intended renewal of our Directors' remuneration policy and long-term incentive arrangements at the start of the year, we commenced a thorough and successful engagement process with proxy advisors and key shareholders together representing over 65% of our register, who strongly supported the proposal that was adapted to their feedback.

In March 2020, following the sudden impact of COVID-19, the proposal for the renewal of the long-term incentive arrangements was withdrawn. Close contact was maintained with shareholders, resulting in an extensive second round of consultation in the autumn in which we contacted over 75% of our register. This follow-on engagement process was both informative and successful, and we believe resulted in a final proposal that was in the interest of all stakeholders, and which was strongly supported at the general meeting of shareholders in January 2021.

Melrose also continued with a variety of workforce engagement initiatives, most notably through its workforce advisory panel ("WAP") which met twice in 2020. Given the Group's decentralised nature and Melrose's strategic business model and regular turnover of businesses, the WAP comprises the Chief Human Resources Officer (or equivalent) from each business unit and a Melrose Group representative. The purpose of the WAP is to promote effective engagement with, and encourage participation from, the Group's workforce.

It is our intention to continue with our programme of stakeholder engagement in 2021. Full detail on how the Board engages with all of its stakeholders and considers them in its decision-making is set out in our Section 172 statement on pages 54 to 57 and in the Sustainability report on pages 58 to 87.

Justin Dowley
Non-executive Chairman
4 March 2021

Governance structure

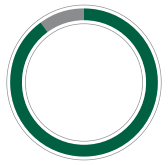
Non-executive Chairman	– Justin Dowley	
Executive Directors	– Simon Peckham – Christopher Miller – David Roper	– Geoffrey Martin – Peter Dilnot (appointed 1 January 2021)
Non-Executive Directors	– Liz Hewitt – David Lis – Archie G. Kane	– Charlotte Twyning – Funmi Adegoke
Audit Committee See page 103	Nomination Committee See page 108	Remuneration Committee See page 124

Diversity and skills overview(1)

Board gender diversity

Male	70%
Female	30%

Board ethnic diversity



Non BAME(2)	90%
BAME(2)	10%

Board skills

Industrial	5
Accounting and Finance	6
Legal	2
Investment	7
Corporate Governance	7

Melrose Executive Committee

Male	65%
Female	35%

Melrose Central employees (excl. Board)

Male	57%
Female	43%

(1) Diversity data as at 31 December 2020. Mr Peter Dilnot was appointed to the Board on 1 January 2021 and it is intended that Mr David Roper will retire at the end of May 2021. The Board is currently recruiting for a new female Non-executive Director.
(2) Black, Asian and Minority Ethnic.

Board of Directors

Justin Dowley
Non-executive Chairman

Year appointed
Appointed as Chairman on 1 January 2019, having previously served as a Non-executive Director from 1 September 2011 and as the Senior Independent Director from 11 May 2017 to 31 December 2018.

Skills and experience
Justin has extensive experience with over 35 years spent within the banking, investment and asset management sector. A chartered accountant, Justin qualified with Price Waterhouse and was latterly Vice Chairman of EMEA Investment Banking, a division of Nomura International PLC. He was also a founder partner of Tricorn Partners, Head of Investment Banking at Merrill Lynch Europe and a director of Morgan Grenfell.

Board meetings attended[1]	4
Business reviews attended	2

Other significant appointments
- Senior Independent Director of Scottish Mortgage Investment Trust PLC
- Director of a number of private companies
- Steward of the Jockey Club
- Deputy Chairman of The Panel on Takeovers and Mergers

Committee membership
- Nomination • Remuneration

Independent	Yes
Tenure[2]	9 years

Christopher Miller
Executive Vice-Chairman

Year appointed
Appointed as Executive Vice-Chairman on 1 January 2019, having previously served as Executive Chairman from May 2003.

Skills and experience
Christopher's long-standing involvement in manufacturing industries and private investment brings a wealth of experience to the Board. A chartered accountant, Christopher qualified with Coopers & Lybrand, following which he was an Associate Director of Hanson PLC. In September 1988, Christopher joined the board of Wassall PLC as its Chief Executive.

Board meetings attended[1]	4
Business reviews attended	2

Other significant appointments
- Trustee of the Prostate Cancer Research Centre

Independent	Not applicable
Tenure[2]	Not applicable

David Roper
Executive Vice-Chairman

Year appointed
Appointed as Executive Vice-Chairman on 9 May 2012, having previously served as Chief Executive from May 2003.

Skills and experience
From a wide range of roles in corporate finance, private investment and management in manufacturing industries, David brings significant investment, financial and operational expertise. A chartered accountant, David qualified with Peat Marwick Mitchell, following which he worked in the corporate finance divisions of S.G. Warburg, BZW and Dillon Read. In September 1988, David was appointed to the board of Wassall PLC, before becoming its deputy Chief Executive in 1993.

Board meetings attended[1]	4
Business reviews attended	2
Independent	Not applicable
Tenure[2]	Not applicable

Simon Peckham
Chief Executive

Year appointed
Appointed as Chief Executive on 9 May 2012, having previously served as Chief Operating Officer from May 2003.

Skills and experience
Simon provides widespread expertise in corporate finance, mergers and acquisitions, strategy and operations. Simon qualified as a solicitor in 1986, before moving to Wassall PLC in 1990, where he became an executive Director in 1999.

Board meetings attended[1]	4
Business reviews attended[3]	1
Independent	Not applicable
Tenure[2]	Not applicable

Geoffrey Martin
Group Finance Director

Year appointed
Appointed as Group Finance Director on 7 July 2005.

Skills and experience
Geoffrey provides considerable public company experience and expertise in corporate finance, raising equity finance and financial strategy. A chartered accountant, Geoffrey qualified with Coopers & Lybrand, where he worked within the corporate finance and audit departments. In 1996, Geoffrey joined Royal Doulton PLC, serving as Group Finance Director from October 2000 until June 2005.

Board meetings attended[1]	4
Business reviews attended	2
Independent	Not applicable
Tenure[2]	Not applicable

Peter Dilnot
Chief Operating Officer

Year appointed
Appointed as an executive Director on 1 January 2021, having served as Chief Operating Officer since April 2019.

Skills and experience
Peter has considerable public company and industrial business experience having been the Chief Executive Officer of international recycling company Renewi plc (formerly Shanks Group plc) and having been a senior executive at Danaher Corporation. Peter also spent seven years at the Boston Consulting Group, working primarily with industrial businesses. Peter has an engineering and aviation background, and was a helicopter pilot in the British Armed Forces. He also holds a degree in Mechanical Engineering.

Board meetings attended[1]	n/a
Business reviews attended	n/a

Other significant appointments
- Non-executive Director of Rotork PLC, and Senior Independent Director of Rotork PLC from 30 April 2021

Independent	Not applicable
Tenure[2]	Not applicable

Liz Hewitt
Senior Independent Director

Year appointed
Appointed as the Senior Independent Director on 1 January 2019, having previously served as a Non-executive Director from 8 October 2013.

Skills and experience
Liz has extensive business, financial and investment experience gained from a number of senior roles in international companies. A chartered accountant, Liz qualified with Arthur Andersen & Co., following which she held a variety of positions within Gartmore Investment Management, CVC and 3i Group PLC. Between 2004 and 2011, Liz was the Group Director of Corporate Affairs for Smith & Nephew PLC, following a secondment to the Department for Business, Innovation and Skills and the HM Treasury, where Liz worked to establish The Enterprise Capital Fund.

Board meetings attended[1]	4
Business reviews attended	2

Other significant appointments
- Non-executive Director of National Grid PLC, Silverwood Property Ltd, St George's Fields Ltd and St George's Fields (No2) Ltd

Committee membership
- Audit (Chairman) • Nomination

Independent	Yes
Tenure[2]	7 years

David Lis
Independent Non-executive Director

Year appointed
Appointed as a Non-executive Director on 12 May 2016.

Skills and experience
David has held several senior roles in investment and fund management, as well as other board appointments. He brings extensive financial experience to the Board. David commenced his career at NatWest, and held positions at J Rothschild Investment Management and Morgan Grenfell after which David founded Windsor Investment Management. David joined Norwich Union Investment Management in 1997 (later merging to form Aviva Investors), before becoming Head of Equities in 2012 and latterly Chief Investment Officer, Equities and Multi Assets, until his retirement in March 2016.

Board meetings attended[1]	4
Business reviews attended	2

Other significant appointments
- Non-executive Director of Electra Private Equity PLC and Dowgate Capital Limited

Committee membership
- Audit • Nomination • Remuneration (Chairman)

Independent	Yes
Tenure[2]	4 years

Archie G. Kane
Independent Non-executive Director

Year appointed
Appointed as a Non-executive Director on 5 July 2017.

Skills and experience
Archie has held several senior roles in the financial services sector and brings extensive financial experience to the Board. Archie qualified as a chartered accountant with Mann Judd Gordon & Company. After a move into the financial services sector as Group Financial Controller of the TSB subsidiary United Dominions Trust, Archie became Group Strategy Director. Archie later served in senior roles for Lloyds Bank and was appointed as CEO of the former mutual Scottish Widows in 2003. In 2009 he moved to become Group Executive Director for all the group's insurance businesses and for Scotland, until his retirement in May 2011. He was also Non-Executive Governor of the Board of the Bank of Ireland until July 2018 and Non-Executive Chairman of Reassure Group plc until July 2020.

Board meetings attended[1]	4
Business reviews attended	2

Committee membership
- Audit • Nomination (Chairman) • Remuneration

Independent	Yes
Tenure[2]	3 years

Charlotte Twyning
Independent Non-executive Director

Year appointed
Appointed as a Non-executive Director on 1 October 2018.

Skills and experience
Charlotte brings a diverse range of experience and commercial acumen to the Board. After a successful legal career specialising in competition and M&A law in the City, she held various senior positions in the telecommunications and transport sectors, most recently in aviation. She has proven leadership skills in large, complex organisations and has consistently succeeded in driving performance and building the foundations for growth.

Board meetings attended[1]	4
Business reviews attended	2

Committee membership
- Audit • Nomination • Remuneration

Independent	Yes
Tenure[2]	2 years

Funmi Adegoke
Independent Non-executive Director

Year appointed
Appointed as a Non-executive Director on 1 October 2019.

Skills and experience
Funmi has extensive experience as a global legal and compliance leader, and has also held senior commercial and project management roles. Having worked in a number of multinationals, and across sectors including aerospace, manufacturing, energy and technology, Funmi brings diverse industrial knowledge and significant commercial expertise to the Board. Funmi is a qualified Barrister, and is currently Group General Counsel at the FTSE 100 company, Halma Plc.

Board meetings attended[1]	4
Business reviews attended	2

Committee membership
- Nomination • Remuneration

Independent	Yes
Tenure[2]	1 year

(1) Meetings attended refers to scheduled meetings.
(2) Tenure runs from the date of appointment until 31 December 2020 and is based on full years only.
(3) With agreement from the Board, Simon Peckham was unable to attend the January 2020 business review due to his attendance at a critical joint venture meeting internationally.

Directors' report

The Directors of Melrose Industries PLC present the Annual Report and financial statements of the Group for the year ended 31 December 2020.

Incorporated information

The Corporate Governance report set out on pages 97 to 102, the Finance Director's review on pages 36 to 42 and the Sustainability report on pages 58 to 87 are each incorporated by reference into this Directors' report.

Disclosures elsewhere in the Annual Report are cross-referenced where appropriate. Taken together, they fulfil the combined requirements of the Companies Act 2006 (the "Act") and of the Disclosure Guidance and Transparency Rules (the "DTRs") and of the Listing Rules of the Financial Conduct Authority.

AGM

The Annual General Meeting of the Company will be held at Leconfield House, Curzon Street, London W1J 5JA at 11.00 am on 6 May 2021. A detailed explanation of each item of business to be considered at the AGM is included with the Notice of Meeting. The notice convening the meeting is shown on pages 208 to 213 and includes full details of the resolutions to be proposed, together with explanatory notes in relation to such resolutions (the "AGM Notice").

Directors

The Directors of the Company as at the date of this Annual Report, together with their biographies, can be found on pages 92 to 93.

Changes to the Board during the year are set out in the Corporate Governance report on pages 97 to 102. Details of Directors' service contracts are set out in the Directors' Remuneration report on page 124.

The Statement of Directors' responsibilities in relation to the consolidated financial statements is set out on page 127, which is incorporated into this Directors' report by reference.

Appointment and removal of Directors and their powers

The Company's articles of association (the "Articles") give the Directors the power to appoint and replace other Directors. Under the terms of reference of the Nomination Committee, any appointment must be recommended by the Nomination Committee for approval by the Board.

Pursuant to the Articles and in line with the UK Corporate Governance Code, all of the Directors of the Company are required to stand for re-election on an annual basis. With the exception of Mr Peter Dilnot, who will be standing for election for the first time following his appointment on 1 January 2021, all current Directors of the Company will be standing for re-election by shareholders at the forthcoming AGM, and in each case an ordinary resolution will need to be passed to approve such (re-)election.

The Directors are responsible for managing the business of the Company and exercise their powers in accordance with the Articles, directions given by special resolution, and any relevant statutes and regulations.

Insurance and indemnities

In accordance with the Articles and the indemnity provisions of the Act, the Directors have the benefit of an indemnity from the Company in respect of any liabilities incurred as a result of their office. This indemnity is provided both within the Articles and through a separate deed of indemnity between the Company and each of the Directors.

The Company has taken out an insurance policy in respect of those liabilities for which the Directors may not be indemnified. Neither the indemnities nor the insurance provides cover in the event that a Director is proved to have acted dishonestly or fraudulently.

Post balance sheet events

There are no post balance sheet events which require disclosure.

Capital structure

The table below shows details of the Company's issued share capital as at 31 December 2019 and as at 31 December 2020.

Share class	31 December 2019	31 December 2020
Ordinary shares of 48/7 pence each	4,858,254,963	4,858,254,963
Incentive Shares (2017)	12,831(1)	12,831(1)

(1) The Incentive Plan (2017) was approved by the Company's shareholders at a general meeting of the Company held on 11 May 2017, and these Incentive Shares were issued pursuant to the authority granted at such meeting to issue Incentive Shares up to an aggregate nominal amount of £50,000. The Incentive Plan (2017) expired in May 2020 for no value, and therefore these incentive shares have no value. The Incentive Shares (2017) will be cancelled by the Company prior to the forthcoming AGM.

The Company's ordinary shares are admitted to the premium segment of the official list.

Shareholders' voting rights

Subject to any special rights or restrictions as to voting attached to any class of shares by or in accordance with the Articles, at a general meeting of the shareholders of the Company, each member who holds ordinary shares in the Company and who is present (in person or by proxy) at such meeting is entitled to:

- on a show of hands, one vote; and
- on a poll, one vote for every ordinary share held by them.

With the exception of the Incentive Shares (2017), which do not carry voting rights (and which will be cancelled by the Company prior to the forthcoming AGM), there are currently no special rights or restrictions as to voting attached to any class of shares.

The Company is not aware of any agreements between shareholders that restrict voting rights attached to the ordinary shares in the Company.

Where any call or other amount due and payable in respect of an ordinary share remains unpaid, the holder of such shares shall not be entitled to vote or attend any general meeting of the Company in respect of those shares. As at 4 March 2021, all ordinary shares issued by the Company are fully paid.

Details of the deadlines for exercising voting rights in respect of the resolutions to be considered at the 2021 AGM are set out in the AGM Notice on pages 208 to 213.

Shareholders whose combined shareholdings amount to at least 5% of the issued voting share capital may, pursuant to section 303 of the Act, request that the Directors call a general meeting of the Company. Shareholders whose combined shareholdings amount to at least 5% of the issued share capital entitled to vote can also request that the Company introduces a resolution to be voted on at an AGM.

Restrictions on transfer of securities

The Articles do not contain any restrictions on the transfer of ordinary shares in the Company, aside from the usual restrictions applicable where shares are not fully paid up, if entitled to do so under the Uncertificated Securities Regulations 2001, where the transfer instrument does not comply with the requirements of the Articles or, in exceptional circumstances, where approved by the Financial Conduct Authority provided such refusal would not disturb the market in such shares. Restrictions may also be imposed by laws and regulations (such as insider trading and market abuse provisions). Directors and certain senior employees of the Group may also be subject to internal approvals before dealing in ordinary shares of the Company and minimum shareholding requirements. We do not have any anti-takeover devices in place, including devices that would limit share ownership.

The Company's incentive shares may only be transferred with the prior written consent of the Board (such consent expressly provided in respect of transfers to personal trusts, companies wholly-owned by the relevant holder and certain of their close relatives).

The Company is not aware of any agreements between shareholders that restrict the transfer of ordinary shares in the Company.

Articles of association

The Articles may only be amended by a special resolution at a general meeting of the shareholders of the Company. There are no amendments proposed to be made to the Articles at the forthcoming AGM.

Substantial shareholdings

As at 31 December 2020, the following voting interests in the ordinary share capital of the Company, disclosable under DTR 5, had been notified to the Directors:

Shareholder	Shareholding	% of ordinary share capital as at 31 December 2020
The Capital Group Companies, Inc	584,610,247	12.03
BlackRock Inc	332,302,037	6.84
Select Equity Group, L.P.	256,129,470	5.27
Aviva Plc	141,906,393	2.92

Between 1 January 2021 and 4 March 2021 no changes to the voting interests in the ordinary share capital of the Company, disclosable under DTR 5, were notified to the Directors.

Shareholder dividend

The Directors are pleased to recommend the payment of a final dividend of 0.75 pence per share (2019: 0 pence) to be paid on 19 May 2021 to ordinary shareholders on the register of members of the Company at the close of trading on 6 April 2021. This dividend recommendation will be put to shareholders at the forthcoming AGM of the Company, to be held on 6 May 2021. Subject to shareholder approval being obtained at the AGM for the final dividend, this will mean a full year 2020 dividend of 0.75 pence per share (2019: 1.7 pence).

For discussion on the Board's intentions with regard to the dividend policy, please see the Chairman's statement on pages 10 to 11, which is incorporated into this report by reference.

The Company offers a Dividend Reinvestment Plan ("DRIP"), which gives shareholders the opportunity to use their dividend payments to purchase further ordinary shares in the Company. Further details about the DRIP and its terms and conditions can be found within the Investors section of the Company's website at **www.melroseplc.net**.

Historical dividends

The Company administers the unclaimed dividends of the former FKI plc (now "Brush Holdings Limited"). Pursuant to law and the company's articles of association, the company is obliged to pay such unclaimed dividends for a period of 12 years from the date on which they were declared or became due for payment. Six months after this time period has expired, the Company's policy is to donate the amount of the unclaimed dividends to a charity of the Company's choice. The amount of unclaimed dividends of the company that surpassed this 12 year threshold during the period was £6,727.33. If the unclaimed dividends are not claimed by 30 June 2021, the Company will look to donate the funds to charity.

Equiniti, the Company's registrar, administers the unclaimed dividends of the former GKN plc (now "GKN Limited"). Pursuant to law and the company's articles of association, the company is obliged to pay such unclaimed dividends for a period of 12 years from the date on which they were declared or became due for payment. The amount of unclaimed dividends of the company that surpassed this 12-year threshold during the period was £26,755.01.

Ability to purchase own shares

Pursuant to sections 693 and 701 of the Act and a special resolution passed at a general meeting of the Company on 7 May 2020, the Company is authorised to make market purchases of up to 485,825,496 of its ordinary shares, representing approximately 10% of the current issued ordinary share capital of the Company. The Company has not made any purchases of its own shares pursuant to this authority.

This authority will expire at the end of this year's AGM, at which the Company is seeking approval to make market purchases of its ordinary shares up to 485,825,496, being approximately 10% of the current issued ordinary share capital, thereby renewing the authority. The full text of the resolution, together with minimum and maximum price requirements, is set out in the AGM Notice on pages 208 to 213.

Financial instruments

The disclosures required in relation to the use of financial instruments by the Company, including the financial risk management objectives and policies (including in relation to hedging) of the Company and the exposure of the Company to liquidity risk, cash flow risk, exchange rate risk, contract and warranty risk and commodity cost risk, can be found in the Finance Director's review on pages 36 to 42, the Risks and uncertainties section of the Strategic Report on pages 46 to 53 and in note 25 to the financial statements, which are incorporated by reference into this Directors' report.

Research and development activities

The industries in which the Group invests are highly competitive and the businesses within the Group are encouraged to research and develop new and innovative product lines and processes in order to meet customer demands in a continuously evolving environment and to support its sustainability goals.

As noted in the Divisional reviews on pages 14 to 33, which are incorporated by reference into this Directors' report, investment into research and development activities continued throughout 2020. GKN Aerospace entered into production on the Wing of Tomorrow programme and initiated a collaboration with Eviation to design and manufacture the wings, aircraft tail and electrical wiring systems for Alice, a ground-breaking regional electric aircraft. In 2021, GKN Aerospace will also commence full operations at its flagship £32 million Global Technology Centre in Filton, UK. For GKN Automotive, its Driveline division continued to develop and expand its product range, executing 36 new programme launches in 2020. On the ePowertrain side, its partnership with Delta Electronics Inc. for the development of advanced eDrive technology, which is set to enhance its existing capabilities in this area, is operating smoothly and we hope will yield positive results in 2021.

The significant investment in innovation and technology at GKN Powder Metallurgy has culminated in the successful validation of its Hy2green technology, which enables hydrogen to be stored locally and from carbon-free renewable energy sources, and can be used in a range of energy storage capacities. The system is expected to be officially launched to market in 2021.

Through continued investment in 2020, Nortek Global HVAC continued to maximise the full potential of technological developments in relation to its StatePoint Technology®. It successfully developed the next iteration of the technology in the form of the HyperScale Data Centre, and further developed its roadmap for future StatePoint Technology® products, to ensure that it remains agile and competitive in the dynamic data centre cooling market.

The Melrose Skills Fund has also funded initiatives in the GKN Aerospace, GKN Automotive and Brush businesses. Further details on the initiatives being implemented are set out in the Sustainability report section of the Strategic Report on pages 58 to 87.

Business review and risks

A review of the Group's performance, the key risks and uncertainties facing the Group and details on the likely development of the Group can be found in the Chairman's statement on pages 10 to 11 and the Strategic Report on pages 1 to 87 of this Annual Report (including the Longer-term viability statement on page 43 and the Risks and uncertainties section on pages 46 to 53), which are incorporated into this Directors' report by reference.

Employee engagement
Details in relation to the workforce advisory panel, employment policies, and employee involvement, consultation and development, together with details of some of the human resource improvement initiatives implemented during 2020, are shown in the Sustainability report and in the Section 172 statement set out in the Strategic Report on pages 54 to 57, both of which are incorporated by reference into this Directors' report.

Business relationships
Details of our businesses' clients and suppliers and how our businesses work and engage with them are described in the Sustainability report on pages 58 to 87, and in the Section 172 statement set out in the Strategic Report on pages 54 to 57, both of which are incorporated by reference into this Directors' report.

Environmental
Details of the Group's environmental initiatives, Greenhouse gas emissions and the methodology used to calculate such emissions are set out in the Sustainability report on pages 68 to 73, which is incorporated by reference into this Directors' report.

Political donations
The Group's policy is not to make any political donations and there were no political donations made during the year ended 31 December 2020 (2019: nil).

Branches
The Melrose Group and its businesses operate across various jurisdictions. The businesses, through their various subsidiaries, have established branches in a number of different countries in which they operate.

Disclosures required under Listing Rule 9.8.4R
Other than the following, no further information is required to be disclosed by the Company in respect of Listing Rule 9.8.4R:

- details of the 2020 Employee Share Plan, which are set out on pages 116 to 117 of the Directors' Remuneration report and note 23 to the financial statements (incorporated by reference into this Directors' report);
- GKN had historically operated employee share option plan trusts to satisfy the vesting and exercise of awards of ordinary shares made under GKN's share-based incentive arrangements. On the acquisition of GKN, these shares were converted into Melrose shares. A dividend waiver is in place on the shareholdings in respect of relevant trusts in part, or in full, in accordance with the provisions of the relevant trust deeds; and
- each member of the Board agreed to a temporary 20% reduction in their salary or base fee (as applicable) in 2020 to support the Company's cash management strategy in light of the COVID-19 crisis.

Significant agreements and change of control
With the exception of the Group's banking facilities, the 2020 Employee Share Plan, and the divisional management long-term incentive plans, there are no other agreements that would have a significant effect upon a change of control of Melrose Industries PLC as at 4 March 2021.

The Group has a committed bank facility, comprising a multi-currency term loan denominated £100 million and US$960 million and a multi-currency revolving credit facility denominated £1.1 billion, US$2.0 billion and €0.5 billion. Details of this facility are provided in the Finance Director's review on page 41 and note 25 to the financial statements.

In the event of a change of control of the Company following a takeover bid, the Company and lenders under the facility agreement are obliged to enter into negotiations to determine whether, and if so how, to continue with the facility. There is no obligation for the lenders to either fund new loans requested during the 30 day period after a change of control, or continue to make the facility available for more than 30 days beyond any change of control. Failure to reach agreement with parties on revised terms could require an acquirer to put in place replacement facilities.

The Company's wholly-owned subsidiary, GKN Holdings Limited, has outstanding £450 million fixed rate notes paying 5.375% p.a. interest and maturing on 19 September 2022 and £300 million fixed rate notes paying 4.625% p.a. interest and maturing on 12 May 2032, in each case issued under Euro medium-term note programmes (together, the "Notes"). Pursuant to the terms and conditions of each of the Notes, a holder of the Notes has the option to require GKN Holdings Limited to redeem or (at GKN Holdings Limited's option) purchase the holder's Notes at their principal amount together with accrued interest, if there is a change of control of GKN Limited and either (i) the Notes are unrated or do not carry an investment grade credit rating from at least two ratings agencies; or (ii) if the Notes carry an investment grade credit rating from at least two ratings agencies, the Notes are downgraded to a non-investment grade rating or that rating is withdrawn within 90 days of the change of control and such downgrade or withdrawal is cited by the ratings agencies as being the result of the change of control.

In the event of a takeover of the Company, awards granted under the 2020 Employee Share Plan would crystallise and convert into ordinary shares in the Company or give rise to an entitlement to a dividend paid in cash. The rate of conversion is based upon the offer price of the Company's ordinary shares as calculated on the date of the change of control of the Company. If the offer price, or any element of the offer price, is not in cash, the Remuneration Committee will determine the value of the non-cash element, having been advised by a reputable investment bank that such valuation is fair and reasonable.

Long-term management incentive plans have been put in place for our key divisions which would be triggered upon a sale of their respective business or a takeover of the Company. The plans provide for the payment of bonuses to certain key managers of these divisions based upon the increase in value of their respective business. If a sale of the relevant business has not occurred within a certain period, the incentive plan will crystallise and any payment to be made to participants will be based on the increase in value of the business during this period.

Commitments
Melrose entered into certain undertakings and other continuing obligations with the UK Government and other regulatory bodies in connection with its acquisition of GKN. It remains in full compliance with these obligations and meets its regular reporting requirements.

Auditor
So far as each Director is aware, there is no relevant audit information (being information that is needed by the Company's auditor to prepare its report) of which the Company's auditor is unaware. Each Director has taken all the steps that he or she ought to have taken as a Director to make him or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Act.

On behalf of the Board, the Audit Committee has reviewed the effectiveness, performance, independence and objectivity of the existing external auditor, Deloitte LLP, for the year ended 31 December 2020 and concluded that the external auditor was in all respects effective. Deloitte LLP has expressed its willingness to continue in office as auditor of the Group. Accordingly, resolutions will be proposed at this year's AGM for the reappointment of Deloitte LLP as auditor of the Group and to authorise the Audit Committee to determine its remuneration.

Approval
Approved by the Board and signed on its behalf by:

Jonathon Crawford
Company Secretary
4 March 2021

Corporate Governance report

In line with the UK Corporate Governance Code (the "Code") and the Listing Rules issued by the Financial Conduct Authority, this section of the Annual Report and financial statements details the ways in which the Company has applied the principles and complied with the provisions of the Code applicable during the year ended 31 December 2020.

The Audit Committee report, Nomination Committee report, Directors' Remuneration report, Statement of Directors' responsibilities, the Risk management and Risks and uncertainties sections of the Strategic Report, together with the Sustainability report and the Section 172 statement, also form part of this Corporate Governance report.

Statement of compliance
Throughout the year ended 31 December 2020, the Company has applied the principles and complied with the provisions of the Code.

1. Principles A-E: Board Leadership and Company Purpose

Long-term sustainable success
The Board is constituted of individuals from a diverse range of backgrounds and with a wealth of knowledge, understanding and experience. The Chairman, with the assistance of the Vice-Chairmen, is responsible for leadership of the Board. The division of responsibilities is described further in section 2 on page 98.

The Board's overarching objective is to generate value for the Company's shareholders in a way that is sustainable in the long term and contributes to wider society. The Section 172 statement on pages 54 to 57 and the Sustainability report on pages 58 to 87 set out the ways in which the Board took these considerations into account in its decision-making in 2020.

Purpose, strategy and values
Melrose was founded in 2003 to empower businesses to unlock their full potential for the benefit of all stakeholders, whilst providing shareholders with an above-average return on their investment. This has been delivered through Melrose's "Buy, Improve, Sell" strategy, which means we buy good quality but underperforming manufacturing businesses and then invest heavily to improve performance and productivity as they become stronger, better businesses under our responsible stewardship. At the appropriate time, we find them a new home for the next stage of their development and return the proceeds to shareholders.

The Company's purpose and strategy are underpinned by the principles and values on which it was founded. We act with integrity, honesty and decisiveness and believe in a lean operating model, high productivity and sustainable business practices. We do not shy away from difficult decisions based on sound financial information, holding people accountable but always treating them fairly. We provide the space and resources to empower people to perform and reward them well when they do. These are the principles that lie at the heart of the success of Melrose and are the basis on which we strive for more success in the future.

Resources and controls
As described in more detail in the Risk management section of the Strategic report and the Audit Committee report on pages 44 to 45 and 103 to 107 respectively, the Board has established a framework of reporting procedures, lines of responsibility and delegated authority, which is updated regularly and understood by all Board members and the Melrose senior management team. These reporting processes allow the Board and Melrose senior management team to allocate resources in a sustainable and appropriate manner, enabling the Group to meet its objectives and measure performance effectively. The Board and the Audit Committee have access to the Melrose senior management team and to external assistance in order to satisfy themselves that appropriate and effective controls are in place.

Stakeholder engagement
Through presentations and regular meetings between the executive Directors, analysts and institutional shareholders, including those following the announcements of the Company's annual and interim results and trading updates, the Company seeks to build on a mutual understanding of objectives with its shareholders. During 2020, in addition to the usual disclosure rounds following the release of annual and interim results, the Company continued its programme of engagement with major investors and corporate governance bodies in respect of specific material topics including the renewal of the Directors' remuneration policy and long-term incentive arrangements, as well as open-agenda discussions between key shareholders and members of the Board. Engagement with key shareholders, proxy advisors, employee bodies, ratings agencies and other governance bodies remains a central part of the Company's approach to stakeholder engagement and governance and shall continue in the lead up to the 2021 AGM. Further details on the Company's engagement with stakeholders are contained in the Section 172 statement on pages 54 to 57 and in the Sustainability report on page 61.

In order to promote effective engagement with, and encourage participation from, its workforce, Melrose operates a workforce advisory panel ("WAP"). Given the Group's decentralised nature and Melrose's strategic business model and regular turnover of businesses, the WAP comprises the Chief Human Resources Officer (or equivalent) from each business unit and a Melrose Group representative. Each member of the WAP is responsible for determining how the workforce should be defined for their respective business unit, promoting workforce engagement, collating the voice of the workforce and demonstrating how that voice is fed into executive decisions for that business unit. The WAP meets twice a year and an annual report is prepared for the Board which highlights workforce engagement and key views. Further details on the WAP are contained in the Section 172 statement on pages 54 to 57.

Workforce policies and practices
Melrose's reputation for acting responsibly plays a critical role in its success as a business and its ability to generate shareholder value. It maintains high standards of ethical conduct which are reflected in the compliance policies that are rolled out to the business units, and cover best practice with respect to anti-bribery and corruption, anti-money laundering, anti-facilitation of tax evasion, competition, conflict minerals, trade compliance, data privacy, whistleblowing, treasury and financial controls, anti-slavery and human trafficking, document retention and joint ventures.

The Company also operates an externally hosted whistleblowing portal which is readily available to all Group employees and supported by regularly updated policies, procedures and awareness campaigns to create an environment in which the workforce feels it is safe to raise concerns in confidence without fear of retaliation, and to foster an ethical and supportive culture within each of the Group's business units. The Board is provided with updates on material whistleblowing events as they are reported from time to time to the Melrose senior management team, and they are provided with an overview of whistleblowing activity on a quarterly basis. An annual report is prepared for the Board which highlights whistleblowing activity in further detail across the business units, together with a summary of the approach taken by each business unit to their whistleblowing process.

2. Principles F-I: Division of Responsibilities

The Board

Details of the structure of the Board and its key responsibilities are shown on pages 62 and 63.

There were four formally scheduled Board meetings held during the year and the attendance of each Director at these meetings is shown on page 99.

Business review meetings are held between scheduled Board meetings. There were two business review meetings held during the year due to the frequency of informal Board meetings held, and the attendance of Directors at these review meetings is set out on page 99. These meetings provide the Directors with a comprehensive understanding of the current performance of, and the key issues affecting, the Group's businesses, without the formality or rigidity of a Board meeting. Divisional CEOs and other senior management from the businesses are periodically invited to attend and present to these meetings, providing the Directors with an opportunity to discuss each business directly and to develop relationships with their leadership teams. The executive Directors also visit the sites of the business units on an ad hoc basis and sessions are held between the executive Directors and the business unit executive teams at such site visits.

During 2020, the regular Board meetings and business review meetings were supplemented by weekly meetings of the Board and weekly cash management meetings with the divisional executive teams during the height of the COVID-19 pandemic in the second and third quarters of 2020. As the initial disruption subsided, these meetings were followed by fortnightly Board meetings and regular key financial information reporting to the Board where necessary. The increased frequency of meetings at Board level enabled the Board to discuss and increase their monitoring and oversight of the financial performance of the Group, particularly in light of the focus on cash generation. It also enabled the Board to have increased monitoring and oversight of the impact of macro-political events on the Group, including national and regional lockdowns, material working pattern changes, and PPE supplies and distribution, and the business units' ongoing assessment and/or use of and paying back of national support schemes where determined appropriate.

Detailed briefing papers containing financial and operational business summaries and an agenda are provided to the Directors in advance of each Board, Committee (where relevant) or business review meeting. The Directors are able to seek further clarification and information on any matter from any other Director, the Company Secretary or any other employee of the Group whenever necessary.

Decisions are taken by the Board in conjunction with the recommendations of its Committees and advice from external consultants, advisors and Melrose senior management.

The Board has a fully encrypted electronic portal, enabling Board, Committee and business review papers to be delivered securely and efficiently to Directors. This facilitates a faster and more secure distribution of information, accessed using electronic tablets and reduced resource usage, which in turn helps to reduce paper waste.

The Company Secretary is responsible for advising and supporting the Chairman and the Board on corporate governance matters as well as assisting the Chairman in ensuring a smooth flow of information to enable effective decision-making. All Directors have access to the advice and services of the Company Secretary and, through him, have access to independent professional advice in respect of their duties, at the Company's expense. The Company Secretary, supported by the Group company secretariat, acts as secretary to the Board, the Audit Committee, the Nomination Committee and the Remuneration Committee.

In accordance with its Articles and in compliance with the Act, the Company has granted a qualifying third-party indemnity to each Director. This indemnity is provided both within the Company's Articles and through a separate deed of indemnity between the Company and each of the Directors. The Company also maintains directors' and officers' liability insurance.

Chairman, Vice-Chairmen and Chief Executive

The roles of each of the Chairman, the Vice-Chairmen and the Chief Executive of the Company are, and will remain, separate in accordance with the Code and Board policy.

The Chairman, with the assistance of the Vice-Chairmen, is responsible for leadership of the Board. The Chairman sets the Board agenda and ensures that adequate time is given to the discussion of issues in order to facilitate constructive discussions with effective contributions from the Non-executive Directors, particularly on those issues of a strategic nature. The Chairman, with the support of the Company Secretary, also facilitates constructive board relations by providing accurate and clear information in a timely manner. Responsibility for ensuring effective communications are made to shareholders rests with the Chairman, the Vice-Chairmen and the three other executive Directors.

The Chief Executive is responsible for strategic direction and decisions involving the day-to-day management of the Company.

Non-executive Directors

The Company's Non-executive Directors are encouraged to, and do, scrutinise the performance of the executive Directors in all areas, including on strategy, risks and financial information, through their roles on the Company's Committees, at the Board's scheduled meetings and business review sessions and on an ad hoc basis. The Non-executive Directors come from a diverse range of backgrounds and as such are able to draw on their own specialist knowledge to give necessary guidance and advice, and hold management to account.

The Board consists of five executive Directors, five Non-executive Directors (inclusive of the Senior Independent Director) and the Non-Executive Chairman. As such, the Board is satisfied that there is sufficient challenge by Non-executive Directors of executive management in meetings of the Board, and that no individual or small group of individuals dominates its decision-making.

Together with the Chairman, each of the Non-executive Directors are members of the Nomination Committee and as such, they play a key role in appointing and removing executive Directors. As considered in section 3, the Non-executive Directors are also key in evaluating the performance of the Directors.

Non-executive Director independence

In accordance with the provisions of the Code, consideration has been given to the independence of all Non-executive Directors. The Board considers all of the Non-executive Directors to be independent.

Upon Mr Justin Dowley's appointment to the role of Chairman of the Board he was considered independent. Ms Liz Hewitt is the appointed Senior Independent Director, and acts as an intermediary for the other Directors and shareholders. In accordance with the Code requirements, at least half of the Board, excluding the Chairman of the Board, comprises Non-executive Directors determined by the Board to be independent. The number of independent Directors on the Board will increase from 50% to 60% (excluding the Chairman of the Board) with the intended retirement of Mr David Roper in May 2021 and the current recruitment process for a new independent Non-executive Director.

Although Mr Dowley has only served as independent Non-executive Chairman since 2019, the Board recognises that he has served as a Non-executive Director for just over nine years, having first joined the Board as an independent Non-executive Director in September 2011. The Code provides that service on the Board for more than nine years from the date of first appointment is a circumstance which may impair independence. In 2019 the Board agreed that Mr Dowley should stay in his position for up to three years beyond 2020, subject to his annual re-election at the Company's AGM, in order to facilitate succession planning arrangements and the development of a diverse Board. This decision had been reached following a positive engagement process with key institutional shareholders on Mr Dowley's tenure. Following strong support for Mr Dowley at the 2020 AGM together with the need to provide stability and certainty in the face of the global pandemic, the Board continues to hold this view.

The Non-executive Directors are not entitled to any cash bonus or shares under the 2020 Employee Share Plan.

Corporate governance framework and terms of reference

The Board has an overarching corporate governance framework to ensure continued alignment of the Board and Committee members' roles and division of responsibilities with the Code, Melrose's top-down Board and senior management risk oversight, and the business units' bottom-up risk management responsibilities. Each member of the Board is provided with a copy of the Company's corporate governance framework, which they review, discuss and update periodically.

Each of the Committees has their own written terms of reference. The Company Secretary supports the Committees in updating these terms of reference in order to comply with the Code and other good corporate practice. The terms of reference are continuously reviewed, although they are more formally reviewed on an annual basis in the Committee meetings. The terms of reference are available via the Melrose website at **www.melroseplc.net**.

Board induction, training and support

An induction programme tailored to the needs of individual Directors is provided for new Directors joining the Board. The primary aim of the induction programme is to introduce new Directors to, and educate them about, the Group's businesses, its operations and its governance arrangements. Individual induction requirements are monitored by the Chairman and the Company Secretary to ensure that new Directors gain sufficient knowledge to enable them to contribute to the Board's deliberations as quickly as possible.

The Board also receives annual training and quarterly updates on key sustainability issues that impact the sectors within which the Group's businesses operate, and on the specific measures that are required to be implemented to drive improved sustainability performance over the longer term for the benefit of all stakeholders.

Time commitments and attendance of Directors at meetings

When considering appointments to the Board, the Board in conjunction with the Nomination Committee reviews any other demands on a candidate's time, and new Directors are required to disclose any directorships held and other business interests. The ability of Directors to have sufficient time to meet their board responsibilities is considered on an annual basis as part of the performance evaluation process. Mr Peter Dilnot is a Non-executive Director of Rotork PLC although the Board has concluded that this does not affect Mr Dilnot's ability to meet his board responsibilities. None of the other executive Directors hold any significant appointments nor do they have any non-executive directorships in any FTSE 100 company.

The following table shows the attendance of each of the Directors at the scheduled meetings of the Board and its Committees held during the year. The quorum necessary for the transaction of business by the Board and each of its Committees is two. The table also shows attendance at business review meetings held between scheduled Board meetings. Non-executive Directors are invited to, but are not required to attend, such meetings.

Attendance of Directors

	Board	Audit	Nomination	Remuneration	Business review
Number of meetings(1)	**4**	**4**	**2**	**2**	**2**
Justin Dowley	4	4	2	2	2
Christopher Miller	4	–	–	–	2
David Roper	4	–	–	–	2
Simon Peckham	4	–	–	–	1(2)
Geoffrey Martin	4	4(3)	–	–	2
Peter Dilnot(4)	–	–	–	–	–
Liz Hewitt	4	4	2	–	2
David Lis	4	4	2	2	2
Archie G. Kane	4	4	2	2	2
Charlotte Twyning	4	4	2	2	2
Funmi Adegoke	4	–	2	2	2

(1) In addition to the above scheduled meetings, ad hoc Board and Committee meetings are held from time to time which are attended by a quorum of Directors and are convened to deal with specific items of business.
(2) With agreement from the Board, Simon Peckham was unable to attend the January 2020 business review due to his attendance at a critical joint venture meeting internationally.
(3) Geoffrey Martin attended by invitation.
(4) Peter Dilnot was appointed as an executive Director with effect from 1 January 2021. Mr Dilnot attended each of the Board meetings and business reviews by invitation.

3. Principles J-L: Composition, Succession and Evaluation

Board composition

The Board believes that the Directors bring a combination of skills, experience and knowledge to the Board that is complementary to the activities of the Company. Biographies of the Directors are shown on pages 62 and 63, and on the Company's website at **www.melroseplc.net**. These biographies identify any other significant appointments held by the Directors.

During the year, Mr Roper had intended on retiring from the Board. However, as a result of the global pandemic, the Board and Nomination Committee agreed that it was not the appropriate time to lose the expertise and experience of one of its co-founders. Mr Roper therefore agreed to delay his retirement to assist the Company in navigating its way through the challenges presented by the pandemic and he will instead retire at the end of May 2021. His knowledge and experience have been very helpful in ensuring the businesses ended the year in a strong position.

Furthermore, as a result of the valuable contribution that Mr Peter Dilnot has made since joining Melrose as Chief Operating Officer in April 2019, the Board appointed Mr Dilnot to the role of executive Director, and such appointment took effect on 1 January 2021. Mr Dilnot brings to the Board a deep understanding of the Melrose business model together with strong sector experience in engineering and aviation.

The Board has made significant progress with paving the way for diversity, including having met the Parker Review target of having one Director from an ethnic minority background on the Board well in advance of the 2021 deadline following the appointment of Ms Funmi Adegoke in October 2019. As at 31 December 2020, Melrose had 30% female representation on its Board, and half of Board appointments between 2016 and 2020 have been female.

Melrose had been on track to achieve the Hampton-Alexander Review target of having 33% female representation on its Board by 2020 with the intended retirement of Mr Roper in May 2020. The Board's decision to delay Mr Roper's retirement was the reason that Melrose did not achieve this goal by the end of last year as had been intended. The middle of the crisis was not the time to lose someone of Mr Roper's experience, but this is now being addressed. Melrose is committed to achieving the Hampton-Alexander Review target in 2021 and along with Mr Roper's retirement it has started the process of recruiting for a new female Non-executive Director. Stonehaven International, an external recruitment consultancy firm unconnected with the Company and its Directors, has been retained to identify suitable candidates for the Board's consideration.

Succession planning

Succession planning is coordinated via the Nomination Committee in conjunction with the Board and includes all Directors and senior management. It was a core focus in 2020 and as explained in section 2 on pages 98 and 99, the Board approved the extension of Mr Dowley's Chairmanship tenure in order to aid effective succession planning.

Succession planning arrangements for the Board as a whole were reviewed by the Nomination Committee and the Board. This included reviewing the skills set, tenure, diversity and independence of those already on the Board, and reviewing the Melrose senior management team including the career planning and talent management programmes in operation for them. In each case this was to allow the Nomination Committee to ensure that the right balance of skills, experience and diversity were reflected and being developed.

Given the strength of Melrose's decentralised operating structure in achieving the Group's strategic objectives, the Nomination Committee does not have direct involvement in the succession planning arrangements of the divisions. However, the Nomination Committee has access to the divisional executive teams through the business review cycle.

Board evaluation

Evaluation approach and process

In accordance with its obligations under the Code to conduct an external Board evaluation at least once every three years, the Board engaged Lintstock Ltd in 2020 to undertake an independent evaluation of the Board, the Audit Committee, the Nomination Committee, the Remuneration Committee, and the Chairman's performance in order to identify areas where performance and procedures might be further improved. Lintstock Ltd is a specialist corporate governance consultancy and, other than the Board, Committee and Chairman evaluations, has no commercial dealings or other connection with the Melrose Group. A range of topics were discussed as part of the evaluation including the Board's adjustment of its focus and priorities in response to the COVID-19 pandemic, the mix of the Board, with diversity of gender, race and thought, succession planning oversight, risk management and internal controls, strategic oversight, understanding of the views and requirements of key stakeholders, and the integration of sustainability into the Group's strategy and operations.

Outputs of the evaluation

The report and subsequent discussion concluded that the Board, the Chairman and the Senior Independent Director continue to be highly effective.

In order to further enhance the Board's effectiveness, the following areas were designated as the subject of management focus during 2021:

- continuing to monitor senior management succession;
- returning to physical meetings for the whole Board;
- further developing the Board's visibility over the impact of principal risks on the divisions, and continuing to monitor and enhance the Group's management of risk;
- further integrating and embedding sustainability into the Group's business strategy and operations, which the Group views as a process of continuous progression in response to ever-evolving sustainability developments;
- although considerable steps were taken to improve cyber security across all business units in 2020, it was recognised that cyber security is an ongoing risk and will, therefore, be focused on again in 2021;
- continuing to improve and monitor the cash management culture within the businesses (particularly within the GKN businesses) and to improve cash performance; and
- continuing to impress upon all divisions that the health and safety of their workers is of utmost importance and ensuring that the divisions' executive teams place a high degree of focus on implementing, monitoring and maintaining high standards of health and safety awareness, coupled with appropriate protective measures and high performance, with a view to eliminating preventable accidents.

Annual re-election of Directors

Pursuant to the Company's Articles and in accordance with the provisions of the Code, all of the Directors stood for election or re-election at the 2020 AGM. With the exception of Mr Dilnot, who is standing for election for the first time, all current Directors of the Company will be standing for re-election by shareholders at this year's AGM and in each case an ordinary resolution will need to be passed to approve such (re-)elections.

In considering whether each Director should stand for re-election, the Nomination Committee in consultation with the Board considers whether the Board has the appropriate balance of skills, experience, independence and diversity to enable the Board to carry out its duties and responsibilities effectively. The time commitments of each Director are also reviewed as part of this assessment, and Directors are required to disclose any directorships held and other business interests. The annual performance evaluation referred to above assists with determining whether each Director should stand for re-election.

Following performance evaluations of each of the Directors, and having considered in turn the individual skills, relevant experience, contributions and time commitment of the Directors to the long-term sustainable success of the Company, the Chairman is of the opinion that each Director's performance continues to be effective and demonstrates commitment to the role. Similarly, following performance evaluations of the Chairman, and having carefully considered the commitments required and the contributions made by the Chairman, the Non-executive Directors, led by the Senior Independent Director, are of the opinion that the Chairman's performance continues to be effective and that he continues to demonstrate commitment to the role.

The justification for Mr Dowley's re-election as Chairman is considered in section 2 on pages 98 and 99.

Mr Simon Peckham, Chief Executive, is standing for re-election as Director due to his deep understanding of the Melrose business model, having joined the Company initially in 2003 as Chief Operating Officer. He has widespread expertise in corporate finance, mergers and acquisitions, strategy and operations.

Mr Christopher Miller and Mr Roper (Vice-Chairmen), are also standing for re-election on the basis of their deep understanding of the Melrose business model, having co-founded Melrose. Mr Miller has long-standing involvement in manufacturing industries and private investment, and Mr Roper (who will retire from the Board at the end of May 2021) has significant financial and operational expertise.

Mr Geoffrey Martin, Group Finance Director, is standing for re-election due to his deep understanding of the Melrose business model, having been appointed as Group Finance Director in 2005. He also brings to the Board considerable public company experience and expertise in corporate finance, equity finance raising and financial strategy.

Mr Dilnot, Chief Operating Officer, is standing for election for the first time. Mr Dilnot brings to the Board a deep understanding of the Melrose business model together with strong sector experience in engineering and aviation.

Ms Hewitt, Senior Independent Director, is standing for re-election as Director due to her extensive business, financial and investment experience gained from a number of senior roles in international companies. In particular, Ms Hewitt is the longest serving Non-executive Director after the Chairman, having served on the Board since 2013, and fulfils the pre-requisite of being independent.

The remaining Non-executive Directors are standing for re-election due to their independence, diversity, skills and experience. In particular, Mr David Lis brings to the Board extensive financial experience and deep insight into the expectations of Melrose's institutional investor base, having held several roles in investment management. Mr Archie G. Kane has extensive financial and general management expertise, having held several roles in the financial services sector and public company boards. Ms Charlotte Twyning brings a diverse range of experience and commercial acumen due to her experience having held various senior positions in the telecommunications and transport sectors, and most recently in aviation. Ms Adegoke brings diverse industrial knowledge as well as significant transactional and commercial management expertise due to her extensive experience working in and leading legal teams across the globe at multi-national organisations.

Biographies of the Directors are shown on pages 62 to 63, and on the Company's corporate website at **www.melroseplc.net**. Detailed justifications for each Director's re-election (or election, as the case may be) are set out in the AGM Notice, on pages 208 to 213.

4. Provisions M-O: Audit, Risk and Internal Control

Objectives and policy

A key responsibility of the Board and Melrose senior management team is to safeguard and increase the value of the businesses and assets of the Group for the benefit of its shareholders. Achievement of their objectives requires the development of policies and appropriate internal control frameworks to ensure the Group's resources are managed properly and that any key risks are identified and mitigated where possible.

The Board is ultimately responsible for the development of the Group's overall risk management policies and system of internal control frameworks and for reviewing their respective effectiveness, while the role of Melrose senior management is to implement these policies and frameworks across the Group's business operations. The Directors recognise that the systems and processes established by the Board are designed to manage, rather than eliminate, the risk of failing to achieve business objectives and cannot provide absolute assurance against material financial misstatement or loss.

The Board is committed to satisfying the internal control guidance for Directors set out in the FRC's Guidance on Risk Management, Internal Control and Related Financial and Business Reporting. In accordance with this guidance, the Board assumes ultimate responsibility for risk management and internal controls, including determining the nature and extent of the principal risks it is willing to take to achieve its strategic objectives (its "risk appetite") and ensuring an appropriate culture has been embedded throughout the organisation. The establishment of a revised risk management and internal control system has been complemented by ongoing monitoring and review, to ensure the Company is able to adapt to an evolving risk environment.

A separate Audit Committee report is set out on pages 103 to 107 and provides details of the role and activities of the Audit Committee and its relationship with the internal and external auditors.

Managing and controlling risk

Since 2016, the Group's approach to risk management has been reviewed and enhanced. The systems, processes and controls in place accord with the Code and the FRC's updated guidance. Details on the Group's risk management strategy are set out on pages 44 to 45.

Further information regarding the Group's financial risk objectives and policies can be found in the Finance Director's review on pages 36 to 42. A summary of the principal risks and uncertainties that could impact upon the Group's performance is set out on pages 46 to 53.

Internal financial controls and reporting

The Group has a comprehensive system for assessing the effectiveness of the Group's internal controls, including strategic business planning and regular monitoring and reporting of financial performance. A detailed annual budget is prepared by senior management and thereafter is reviewed and formally adopted by the Board.

The budget and other targets are regularly updated via a rolling forecast process and regular business review meetings are held with the involvement of senior management to assess performance. The results of these reviews are in turn reported to, and discussed by, the Board at each meeting. As discussed in the Audit Committee report on pages 103 to 107, the Group engages BM Howarth as internal auditor. A total of 28 internal audit physical site visits were completed by BM Howarth and Ernst & Young during 2020 across the Group. As was common across most large, geographically dispersed companies during 2020, COVID-19 disruption presented a number of challenges and limitations due to restricted international travel and extended periods of remote working for many site-based finance teams. Further details about the additional assurance measures that were taken to mitigate the impact of COVID-19 disruption on internal controls during 2020 can be found in the Audit Committee report on pages 103 to 107.

The Directors can report that based on the sites visited and reviewed in 2020, there has been progress across the Group following the 2020 internal audit programme and that the majority of the recommendations presented in the internal audit report have been or are in the process of being implemented.

The Audit Committee also monitors the effectiveness of the internal control process implemented across the Group through a review of the key findings presented by the external and internal auditors. Management are responsible for ensuring that the Audit Committee's recommendations in respect of internal controls and risk management are implemented.

Compliance and ethics

The Company takes very seriously its responsibilities under the laws and regulations in the countries and jurisdictions in which the Group operates and has in place appropriate measures to ensure compliance. A compliance framework is in place comprising a suite of policies relating to anti-bribery and anti-corruption, anti-money laundering, anti-facilitation of tax evasion, competition, conflict minerals, trade compliance, data privacy, whistleblowing, treasury and financial controls, anti-slavery and human trafficking, document retention and joint ventures. These policies are in place within each business and, other than in respect of certain policies where it would not be appropriate for them to have such a broad reach, they generally apply to all Directors, employees (whether permanent, fixed-term, or temporary), pension trustees, consultants and other business advisors, contractors, trainees, volunteers, business agents, distributors, joint venture partners or any other person working for or performing a service on behalf of the Company, its subsidiaries and/or associated companies in which the Company or any of its subsidiaries has a majority interest.

Melrose Industries PLC Annual Report 2020

During 2020, the Melrose Code of Ethics and Group compliance policies were updated to bring them up to date with key regulatory and legal developments and to align more closely with the Group's sustainability principles. They have been fully implemented across all business units together with refreshed risk assessment guidance, and they continue to be monitored to ensure their effectiveness for the Group. The Group also introduced its first Group-wide conflict minerals policy, and further details about this can be found on page 67 of this Annual Report. Online compliance training continued to be conducted within all businesses, covering topics such as anti-trust, trade compliance and export controls, data privacy, anti-bribery and anti-corruption and anti-money laundering, to enhance and supplement the existing compliance regime.

The Company's Modern Slavery Statement is approved by the Board annually and the current statement is available on the Company's website at **https://www.melroseplc.net/media/2568/modern-slavery-statement-june-2020.pdf**. Under Melrose's decentralised group structure, each division is responsible (where applicable) for publishing their own Modern Slavery Statements in accordance with the requirements under the Modern Slavery Act 2015 and are supported by Melrose where needed. To support the Company's belief in the importance of this matter, it has a Group-wide policy on the prevention of modern slavery and human trafficking, which the businesses have rolled out to employees, along with an online compliance training module. Please also refer to section 1 on page 97 for details of the Company's whistleblowing policies and procedures.

BDO LLP have been engaged to conduct an independent non-financial review programme of the GKN Aerospace and GKN Automotive divisions, to test and provide additional external assurance in respect of those businesses' key compliance areas and safeguards as a result of their relative scale and complexity. COVID-19 travel restrictions have caused some delay to the original site visit schedule. However, site visits recommenced during the fourth quarter of 2020. A total of 37 physical site visits were conducted in 2020, which included GKN Aerospace sites across the UK, Netherlands, India, Singapore, Thailand, Sweden, and Norway, as well as GKN Automotive sites including those located in Mexico, France, Malaysia, Germany, Italy, India and Japan.

5. Provisions P-R: Remuneration

Policies and practices

Melrose's remuneration philosophy has been the same since being founded in 2003 and requires that executive remuneration be simple and transparent, support the delivery of the value creation strategy, and pay only for performance. The Company's policy of restricting opportunity in annual salary, bonus and benefits to below the lower quartile of its peers, while heavily weighting potential reward to the long-term employee share plan that is entirely performance based, reflects those principles and is intended to align management's incentive arrangements directly with the interests of shareholders. In compliance with the Code, the 2020 Employee Share Plan (which is the only share plan the Company operates for management) has a five-year total vesting and holding period, which promotes long-term sustainable success for shareholders, and is also expected to be awarded in shares, further aligning management with shareholders.

Development of policies

The Remuneration Committee has a formal and transparent procedure for developing the policy on executive remuneration. It regularly engages with shareholders to seek their views (and particularly more so in advance of renewals), takes those views into account when formulating proposals on executive remuneration, obtains advice from external remuneration advisors, and undertakes benchmarking exercises with respect to executive pay to ensure that the executive remuneration structure remains accurate. Shareholders have the opportunity to vote on executive remuneration through their binding vote at least every three years on the Directors' remuneration policy and their advisory vote annually on the Directors' remuneration report. As described further in the Directors' Remuneration report, the Chief Executive retains responsibility for setting and managing the remuneration of Melrose senior management and divisional CEOs, of which the Remuneration Committee has full disclosure. No Director is involved in deciding their own remuneration outcome.

Independent judgement and discretion

The Directors exercise independent judgement and discretion when authorising remuneration outcomes, taking account of both Company and individual performance, and wider circumstances. As mentioned above, the Remuneration Committee obtains regular advice from external remuneration advisors in order to ensure that proposals are in line with the Code, and benchmarked against the FTSE 100. The current Directors' remuneration policy provides the Remuneration Committee with the ability to exercise discretion to override formulaic outcomes.

Details regarding Directors' remuneration, both generally and in relation to the requirements of the Code, are set out in the Directors' Remuneration report on pages 110 to 126, which is presented in the following two sections:

- the annual statement from the Chairman of the Remuneration Committee, which can be found on pages 110 to 111; and
- the Annual Report on Remuneration, which can be found on pages 112 to 126.

The current Directors' remuneration policy, which was approved by shareholders at the 2020 AGM and subsequently amended in January 2021 to incorporate the 2020 Employee Share Plan, is available on the Company's website[1].

(1) The full details of the Directors' Remuneration Policy can be found on pages 103 to 111 of the 2019 Annual Report (**www.melroseplc.net/media/2536/melrose-ar2019.pdf**), and the full details of the amendments can be found on pages 15 to 24 of the circular to shareholders dated 29 December 2020 (**www.melroseplc.net/media/2587/291220-melrose-circular.pdf**).

Audit Committee report

The responsibilities of the Audit Committee (the "Committee") include overseeing financial reporting, risk management and internal financial controls, in addition to making recommendations to the Board regarding the appointment of the Company's internal and external auditors.

Liz Hewitt
Audit Committee Chairman

Member	No. of meetings[1]
Liz Hewitt (Chairman)	4/4
David Lis	4/4
Archie G. Kane	4/4
Charlotte Twyning	4/4

(1) In addition to the usual scheduled three meetings per year, an additional Committee meeting was held in June 2020 to review the Group's control environment during the COVID-19 pandemic. In addition to the four Committee meetings, all Committee members attended weekly meetings of the Board backed up by weekly cash management meetings during the initial height of the pandemic to ensure close oversight of critical issues across the Group, including a higher frequency of review with respect to the Group's controls, which were followed by fortnightly meetings and regular key financial information reporting where necessary.

Role and responsibilities

The Committee's role and responsibilities are set out in its terms of reference. These were updated in November 2020 in line with best practice and are available on the Company's website at **www.melroseplc.net** and from the Company Secretary at the Company's registered office. In discharging its duties, the Committee embraces its role of protecting the interests of all stakeholders with respect to the integrity of financial information published by the Company and the effectiveness of the audit. The responsibilities of the Committee include:

- reviewing and monitoring the integrity of the financial statements of the Group, including the Annual Report and financial statements and interim financial statements, and reviewing and reporting to the Board on significant financial reporting issues and judgements which they contain;
- keeping under review the effectiveness of the Group's financial reporting;
- reviewing the effectiveness of and monitoring and overseeing the Group's risk management (excluding cyber security and fraud risk, which are retained by the Board), internal financial control systems and processes and compliance controls;
- overseeing the adequacy and security of the Company's arrangements for its employees to raise concerns in confidence in accordance with the Company's whistleblowing policy, including about possible wrongdoing in financial reporting or other matters;
- monitoring and evaluating the independence and effectiveness of the internal audit function and approving the internal audit plan and fee;
- monitoring and evaluating the independence and effectiveness of the external audit and approving the external audit plan and fee;
- reviewing, challenging and reporting to the Board on the going concern assumption and the assessment forming the basis of the longer-term viability statement;
- reviewing and where necessary challenging the consistency of accounting policies, and methods used to account for significant or unusual transactions, and compliance with accounting standards;
- reviewing the Company's procedures for detecting fraud, and its systems and controls for the prevention of bribery;
- developing, implementing and monitoring the Group's policy on external audit and overseeing the objectivity and effectiveness of the external auditor;
- assessing annually the external auditor's independence and objectivity, taking into account relevant UK law, regulation, the Ethical Standards and other professional requirements and the relationship with the auditor as a whole, including the provision of any non-audit services;
- reviewing and where necessary challenging the provision of non-audit services by the external auditor; and
- reviewing and considering the Annual Report and financial statements to ensure that it is fair, balanced and understandable and advising the Board on whether it can state that this is the case.

Composition

Ms Liz Hewitt continues to serve as the Chairman of the Committee. Ms Hewitt and Mr Archie G. Kane bring their significant and relevant financial experience to their roles on the Committee. Furthermore, each member of the Committee including Mr David Lis and Ms Charlotte Twyning brings strong corporate governance experience to the Committee. Further details of the relevant experience of each member of the Committee is described in their biographies on pages 92 to 93. The Committee is made up 100% of independent Non-executive Directors.

The Company Secretary acts as secretary to the Committee.

To enable the Committee to provide robust challenge of the reports submitted to it, the Committee invites the Group Finance Director, the Head of Financial Reporting and senior representatives of the external and internal auditors to attend its meetings. The Committee has the right to invite any other Directors and/or employees to attend meetings where this is considered appropriate. In addition, the Committee meets at least once per year with the external and internal auditors without management present, and the Chairman of the Committee speaks with the external and the internal auditors prior to each Committee meeting.

Audit Committee report

Continued

Summary of meetings in the year

The Committee is expected to meet not less than three times a year. In 2020, the Committee met in March, September and November. The scheduling of these meetings is designed to be aligned with the financial reporting timetable, thereby enabling the Committee to review the Annual Report and financial statements, the interim financial statements and the audit plan ahead of the year-end audit and to maintain a view of the internal financial controls and processes throughout the year.

In addition to the three scheduled meetings, in June 2020 the Committee met to review the Group's control environment during the COVID-19 pandemic, which included:

- review and challenge of the approach taken to internal audit as a result of the travel disruption caused by the pandemic;
- consideration of the closer monitoring and tighter controls measures implemented across the Group, including increased frequency of review of Group controls over cash reporting and trading results from monthly to weekly to ensure that appropriate challenges were being made and addressed almost on a real-time basis, and that key decisions were supported by the Group all the way through to Board level;
- review of the Group's response to the UK Financial Reporting Council's ("FRC") guidance and emerging market practice to separately disclose specific balance sheet implications from COVID-19 in accordance with the Group's existing policy for 'adjusting items'; and
- re-evaluation of operational controls to ensure that any additional risks as a result of COVID-19 were being considered and where possible addressed.

Given the ongoing uncertainty and disruption caused by COVID-19, the Committee has scheduled four meetings in 2021 to enable further review and challenge of significant accounting matters.

Significant activities related to the 2020 financial statements

As part of its duties the Committee undertook the following recurring activities that receive annual scrutiny:

- review of the 2020 Annual Report and financial statements and the interim financial statements, including the going concern of the Group assumption and the assessment forming the basis of the longer-term viability statement. As part of this review, the Committee received reports from the external auditor on their audit of the Annual Report and financial statements and their review of the interim financial statements, as well as papers prepared by management in respect of the going concern and long-term viability and significant accounting and control matters from management;
- consideration of the Annual Report and financial statements in the context of being fair, balanced and understandable and a review of the content of a paper prepared by management in relation to the 2020 Annual Report and financial statements. The Committee advised the Board that, in its view, the 2020 Annual Report and financial statements when taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy;
- review of the effectiveness of the Group's risk management and internal financial controls, impacted by remote working and disclosures made in the 2020 Annual Report and financial statements on this matter;
- review of the effectiveness of the Group's internal and external auditors; and
- review of and agreement of the scope of work to be undertaken in respect of the 2020 financial statements by the external auditor and the scope of work to be undertaken in 2021 by the internal auditor.

In addition to these matters, the Committee considered the following significant issues in relation to the financial statements during the year:

The Audit Committee's activities during 2020

Significant issue considered by the Audit Committee	How the issue was addressed by the Audit Committee
Impairment testing of goodwill Impairment testing is inherently subjective as it includes assumptions in calculating the recoverable amount of the cash-generating unit ("CGU") being tested. Assumptions include future cash flows of the relevant CGU, discount rates that reflect the appropriate risk and long-term growth rates which are applicable to the geography of operations. During 2019, the Group disclosed additional sensitivities for Nortek Control, following an impairment charge, and the Powder Metallurgy and Automotive Driveline groups of CGUs due to global automotive market decline at that time. During 2020, the COVID-19 global pandemic had a significant impact on the global end markets in which certain of the Group's businesses operate with a sharp decline in revenue during the second quarter. During the second half of the year, there was an improvement in trading conditions for most businesses, however, there remains a range of possible outcomes around the speed of future recovery of end markets. Due to the impact of COVID-19, the businesses have mitigated the impact of lower levels of demand through cost reduction and efficiency actions, including significant restructuring. Under IAS 36, the value in use basis prohibits the inclusion of benefits from future uncommitted restructuring plans although this is permitted when applying the fair value less costs to sell basis, to the extent that similar actions would be carried out by a market participant. Due to the timing of impairment testing a fair value less costs to sell approach has resulted in higher valuations than the value in use approach for certain, but not all, groups of CGUs. As disclosed in 2019, there has been a change to the Aerospace group of CGUs in the year, following the announcement of a new operating model in the business. This new CGU structure, comprising Engine Systems and Aerostructures, was effective from 1 January 2020. A further change in both the Aerospace and Automotive groups of CGUs took place with effect from 1 November 2020, resulting from the implications of organisational structural changes and the impact of COVID-19. Rather than two groups of CGUs in each of Aerospace and Automotive, there is now one group of CGUs within each business. *(Refer to notes 3 and 11 of the financial statements)*	The Committee challenged the outcome of the impairment review in respect of all groups of CGUs and particularly where headroom was considered low, and also considered the proposed disclosures in respect of the Aerospace Engine Systems, Aerospace Aerostructures, Automotive Driveline, Automotive ePowertrain, Powder Metallurgy, Ergotron and Nortek Control groups of CGUs, given their sensitivity to reasonably possible changes in assumptions. In doing so the Committee considered the following: • a paper prepared by management, which included the key outputs from the impairment models; • the trading assumptions, including macro-economic factors, applied in the models and in particular those that were key, being revenue growth and operating margin; • the market-based assumptions for the long-term growth rates and the discount rate; • risk adjustments that were applied to the model, in particular regarding the extent of market decline and timing of when volume reductions would recover; and • the appropriateness of the full disclosures in the financial statements in respect of the impairment review performed and the impact, together with sensitivities that could cause a future impairment. The Committee discussed with Deloitte the audit work performed by them and their conclusion regarding the disclosures presented. Considering all of the above, as well as management responses to challenge and Deloitte's views, the Committee was satisfied that the assumptions used were reasonable and that the impairment conclusions together with disclosures were appropriately presented.

The Audit Committee's activities during 2020

Significant issue considered by the Audit Committee	How the issue was addressed by the Audit Committee
Going concern and viability The Committee is required to make an assessment of the going concern assumptions for the Group and the basis of the viability statement before making a recommendation to the Board. The assessment of going concern for the annual financial statements uses the same forecast data as included in many other areas of estimation within the full year accounting and takes into account the revised covenant tests agreed with the Group's banking syndicate during the year. *(Refer to note 2 of the financial statements)*	The Committee reviewed and approved management's recommendation to prepare the financial statements on a going concern basis. The key principles debated were the level of committed facility headroom on bank covenants and flexibility of liquidity arrangements to meet obligations. In addition to base case modelling which uses approved financial forecasts, a reasonably possible downside was considered. The Committee also considered a paper and financial model prepared by management in respect of the longer-term viability statement to be included in this Annual Report and financial statements as well as analysis conducted by the external auditor. The additional period beyond the going concern review of twelve months meant that refinancing events were also considered in the context of future available finance to the Group. The Committee challenged the assumptions and judgements made by management before concluding that the longer-term viability statement was appropriate.
Provisions for loss-making contracts The level of provisioning for loss-making contracts requires estimation and assumptions for long-term programmes. Although provisions are reviewed on a regular basis and adjusted for management's best views, their inherently subjective nature means that future amounts settled may be different from those provided. During the year, as a result of a continued focus on improving profitability through operational actions or enhancing commercial terms with customers, a number of contracts have successfully become break-even or better. There has been a consequential net release of provisions of £95 million, recorded as an adjusting item to avoid positively distorting adjusted operating profit. *(Refer to notes 3, 6 and 21 of the financial statements)*	At 31 December 2020, the carrying value of loss-making contract provisions in the Group was £246 million (2019: £384 million). The Committee considered management's position and challenged the proposed changes during the year as well as the closing provisions. The key assumptions and estimates include volumes, price and costs to be incurred over the life of the contract and, where changes have occurred in commercial terms, relevant legal advice. Deloitte also reported on loss-making contract provisions to the Committee. Having considered the matters presented and responses to challenge, the Committee concluded that management's proposed provisioning, released amounts and the associated disclosures in the financial statements were appropriate and the approach taken was consistent with previous years.
Accounting for revenue under IFRS 15 Following the Group's adoption of IFRS 15 "Revenue from Contracts with Customers" in 2018, management continue to monitor the key assumptions used within the GKN Aerospace business, specifically regarding recognition of variable consideration for risk and revenue sharing partnerships ("RRSPs"). The reduction in activity in the year led to significantly less variable consideration recognised of £13 million (2019: £45 million). The additional controls which were introduced by management in light of the complex commercial arrangements, evolving programme matters and dynamic market conditions have continued to be robust in the year. *(Refer to notes 3, 4 and 17 of the financial statements)*	The Committee discussed with management the ongoing implications of IFRS 15, which included an assessment of estimates used in calculating variable consideration within RRSPs. The Committee discussed the audit work performed by Deloitte, to assess whether the proposed revenue to be recognised, together with incremental disclosures, were appropriate. The Committee was satisfied that the approach and assumptions used remained both reasonable and appropriate. However, it is understood that there are reasonably possible changes in assumptions, that could lead to the recognition of further variable consideration in the next year in respect of previous performance obligations.
GKN Aerospace North America financial information in relation to inventory balances The Group has again reviewed the inventory balances in GKN Aerospace North America following historical pre-acquisition concerns, to ensure that balances were appropriately stated. The current year review has been less intrusive into the business than previously, with assurance taken from necessarily higher-level procedures. The review focused on inventory provisioning, as these calculations often require judgement by management of the expected value of future sales. *(Refer to notes 3 and 16 of the financial statements)*	During the year, the Committee reviewed a report updating on the previously disclosed concerns relating to GKN Aerospace's North American business. The assessment considered trends in inventory carrying amounts and other balance sheet accounts as well as the overall control environment and progress since the prior year. Specifically, senior management from the Group finance team met with site management as well as senior members of divisional finance and governance functions to discuss the local control environment, any impact of COVID-19 on compliance and documentation and results of year-end balance sheet review work. The Committee discussed the results from year-end testing with management as well as the findings from Internal Audit. Additionally, the Committee sought a view from Deloitte following their audit work, to assess whether the balances included in the Group consolidated financial statements were appropriate. Having considered the matters presented and evidence provided, the Committee concluded that management's response to issues was appropriate and balances were reasonably stated.
Classification of adjusting items and use of Alternative Performance Measures ("APMs") The reporting, classification and consistency of adjusting items continues to be an area of focus for the Committee, in particular, given the guidance on APMs provided by the European Securities and Markets Authority ("ESMA"). The Committee considers this a key consideration when reviewing if the financial statements are fair, balanced and understandable. *(Refer to notes 3 and 6 of the financial statements)*	The Committee has considered the nature, classification and consistency of adjusting items, whilst addressing the guidance provided by ESMA. These items are defined and discussed in the Finance Director's review and detailed in note 6 to the financial statements together with the glossary to the financial statements. Following a review of management's paper and challenge, the Committee is satisfied that there has not been any change in substance of the policy. It was noted that the impact of the COVID-19 global pandemic had required management to review the carrying values of operating assets within the Group. A charge of £159 million relating to fixed assets, and £25 million relating to other net operating assets, mostly in the second quarter of the year within the Aerospace division, was recorded to reflect new levels of industry demand. The Committee also determined that disclosures are clear and transparent, assisting shareholders in measuring the operating performance of the Group. The Committee therefore concluded that adjusting items were appropriately captured and disclosed. The Committee also considered disclosure of the Group's APMs with respect to applicable guidelines and noted that these are set out in detail in the glossary to the financial statements together with reconciliations of adjusted performance measures to statutory results in note 6 to the financial statements. The Committee found the disclosures to be clear and transparent.

Audit Committee report
Continued

Risk management and internal control

During 2020, the Committee continued to keep under review the Company's internal financial controls systems that identify, assess, manage and monitor financial risks and other internal control and risk management systems, and the effectiveness of the Group's risk management system, through regular updates from management. This included a review of the key findings presented by the external and internal auditors having agreed the scope, mandate and review schedule in advance.

During 2020, management with support from Ernst & Young consolidated the businesses' risk reporting to the Company using the online interactive dashboard that was developed in 2019. Since the rollout of the dashboard, the Group risk management processes, reporting and data collection from the businesses have continued to be enhanced, in order to bolster the Committee's oversight of risk areas and trends. The dashboard includes data from the risk registers prepared by the risk and legal leads from each business, as well as objective trend analysis based on that data and independent insight from Ernst & Young. The Committee reviewed and challenged the process of compiling the dashboard, as well as a summary report of the Group enterprise risk management profile which guided the Committee on relevant updates to the Group risks as reported in the Risks and uncertainties section on pages 46 to 53, and set out a consolidated risk profile report for each business within the Group.

Management also reported on the Group's internal control systems supported by the internal audit review. Samples of both Group and business unit controls, including financial, operational and compliance controls, were presented and examined.

The Group's risk management and internal financial control systems were reviewed and the Committee confirmed their effectiveness. No significant weaknesses were identified. The Committee reported its conclusions to the Board at the next scheduled Board meeting.

Committee evaluation

The UK Corporate Governance Code requires that FTSE 350 companies undertake a formal and rigorous annual evaluation of the performance of the Board, its committees, the Chair and individual Directors. In particular, FTSE 350 companies should undertake an externally facilitated Board and Committee evaluation once every three years. The last external Melrose Board and Committee review was in 2017, and so the Company was required to undertake another in 2020. For this purpose, the Company engaged Lintstock Ltd who engaged directly with the Directors on (i) the constitution and performance of the Board and each Committee; (ii) the Chairman of the Board; and (iii) individual performance reviews. Lintstock Ltd produced a report based on the feedback of Committee members and analysis of the responses, which was presented and discussed at the December Board meeting. Alongside such formal feedback, the Committee continued to facilitate direct ongoing contact between its members and the Chairman of the Committee about any relevant matters that the members wish to raise as part of the ongoing review.

External audit

Assessment of effectiveness and reappointment

The Committee reviews and makes recommendations with regard to the reappointment of the external auditor. In making these recommendations, the Committee considers auditor effectiveness and independence, partner rotation and any other factors which may impact the external auditor's reappointment.

The Committee has reviewed the external auditor's performance and effectiveness. For 2020, a series of questions covering key areas of the audit process that the Committee is expected to have an opinion over were considered by the Committee, including:

- the calibre, experience, resources, leadership and technical and industry knowledge of the engagement partner and of the wider external audit team;
- the planning and execution of the audit process;
- the quality and timeliness of communications from the external auditor; and
- the quality of support provided to the Committee by the external audit partner.

Committee members, together with the Group Finance Director and the divisional finance directors, were requested to provide detailed feedback on the effectiveness of the external auditor. The Chairman of the Committee also sought feedback from the Chief Executive and the internal auditor. The Company Secretary subsequently produced a paper summarising the responses, which was considered by the Committee at length. The Committee subsequently concluded that the quality of the external audit team remains very high, the external audit process is operating effectively and Deloitte LLP continues to prove effective in its role as external auditor.

FRC Audit Quality Review

The FRC's Audit Quality Review team selected to review the audit of the 2019 Melrose Industries PLC financial statements as part of their annual inspection of audit firms. The FRC review covered selected aspects of the audit only and focused on identifying areas where improvements were required. The Chairman of the Committee received a full copy of the findings from the Audit Quality Review team and has discussed these with Deloitte. The Committee confirmed that there were no significant areas for improvement identified within the report and was satisfied that there is nothing within the report which might have a bearing on the audit appointment. As detailed below, the Committee regularly monitors the objectivity and independence of the external auditor. Deloitte LLP was appointed in 2003 when the Company commenced trading and the external audit has not been formally tendered since then. The Committee is satisfied that the effectiveness and independence of the external auditor is not impaired in any way.

Audit tendering

The Committee has considered audit tendering provisions outlined in the Code. The Committee has also reviewed the regulations provided by the European Commission (as they form part of retained UK law) and the Competition and Markets Authority ("CMA"). The Committee understands that rotation of the external audit firm is required by 2024. The Committee's intention is to put the external audit out to tender in accordance with the relevant timeframes.

The current audit engagement partner was appointed in 2019. The Company's audit firm is required to be rotated by 2024. Therefore, the new audit engagement partner will serve a full five-year term for the Group until the firm rotation in 2024.

Non-audit services

Under CMA and EU regulations (as they form part of retained UK law), there are restrictions on the type and amount of non-audit services provided by Deloitte, which cap the level of permissible non-audit services awarded to the external auditor at 70% of the average audit fee for the previous three years. The cap applies in respect of the current financial year, with audit fees in 2017, 2018 and 2019 being relevant.

A policy on the engagement of the external auditor for the supply of non-audit services is in place to ensure that the provision of non-audit services does not impair the external auditor's independence or objectivity. The policy outlines which non-audit services are pre-approved (being those which are routine in nature, with a fee that is not significant in the context of the audit or audit-related services), which services require the prior approval of the Committee and which services the auditor is excluded from providing. The general principle is that the audit firm should not be requested to carry out non-audit services on any activity of the Company where the audit firm may, in the future, be required to give an audit opinion. In accordance with best practice FRC guidelines, the Company's policy in relation to non-audit services is kept under regular review and was updated in 2020 to reflect current market practice.

Despite being well within the CMA guidance, the Committee has taken into account feedback from institutional shareholder services and has continued migrating non-audit work to other firms and has recently worked with Ernst & Young and KPMG in respect of corporate finance affairs and risk management and obtained reward, tax, consulting advice and advice on the remuneration reporting regulations and preparation of the Directors' Remuneration report from PwC LLP.

During 2020, the main non-audit services provided by Deloitte LLP were in relation to non-statutory audits of carve-out financial statements, assurance reports for government grants or subsidies and tax compliance in non-EU subsidiaries. The Company did not use Deloitte LLP for any significant taxation services and does not intend to in the future. The Company's non-audit fee paid to the external auditor of £1.93 million represents 21.8% of the audit fees for 2020.

The Committee closely monitors the amount of non-audit work undertaken by the external auditor and considers using other firms for transaction-related work. However, there are occasions when it is appropriate, because of background knowledge, to use the auditor for non-audit work, for example on certain compliance projects.

An analysis of the fees earned by the external auditor for audit and non-audit services can be found in note 7 to the consolidated financial statements.

Auditor objectivity and independence

The Committee carries out regular reviews to ensure that auditor objectivity and independence are maintained at all times. As in previous years, the Committee specifically considered the potential threats that each limited non-audit engagement may present to the objectivity and independence of the external auditor. In each case, the Committee was satisfied with the safeguards in place to ensure that the external auditor remained independent from the Company and its objectivity was not, and is not, compromised. No fees were paid to Deloitte LLP on a contingent basis.

At each year end, Deloitte LLP submits a letter setting out how it believes its independence and objectivity have been maintained. As noted above, Deloitte LLP is also required to rotate the audit partner responsible for the Group audit every five years and significant subsidiary audits every five years.

Based on these strict procedures, the Committee remains confident that auditor objectivity and independence have been maintained.

Internal audit

Due to the size and complexity of the Group, it is appropriate for an internal audit programme to be used within the business. BM Howarth Ltd, an external firm, provides internal audit services to the Group in accordance with an annually agreed Internal Audit Charter and internal audit plan. Where additional or specific resource is required, additional support is provided by Ernst & Young. A rotation programme is in place, such that every business unit site will have an internal audit at least once every three years, with the largest sites being reviewed at least once every two years. The rotation programme allows divisional management's actions and responses to be followed up on a timely basis. The internal audit programme of planned visits is discussed and agreed with the Committee during the year.

The internal auditor's remit includes assessment of the effectiveness of internal financial control systems, compliance with the Group's Policies and Procedures Manual and a review of the businesses' balance sheets. A report of key findings and recommendations is presented to Melrose senior management, including the Head of Financial Reporting, followed by a meeting to discuss these key findings and to agree on resulting actions.

As a result of the COVID-19 global pandemic, the internal audit programme for 2020 was reassessed in the first half of the year as restrictions on site access were necessary and there was a reduced ability to travel. After a near full programme in the first quarter, there was little activity in the second quarter due to site closures and certain staff on temporary leave. During the second half of the year, the internal audit programme was adapted to reflect an achievable level of activity, acknowledging the ongoing implications from the global pandemic. The balance between assurance sought from the internal audit programme and other areas of internal control was considered by the Committee in setting a revised schedule of internal audit site visits along with additional procedures for senior management to conduct, thus allowing the Committee to fulfil its obligations with regard to internal control. Site visits during the second half of the year were conducted through a mix of remote working and physical presence where possible such that a total of 28 sites were assessed in 2020.

To supplement the internal audit programme, a targeted sample of sites was selected for a balance sheet review with interviews of site controllers conducted by the internal auditor and senior management, together with self-certification questionnaires which were discussed in detail with divisional finance directors at the internal control sign-off meetings. A report of all significant findings is presented by the internal auditor to the Committee at each meeting and implementation of recommendations is followed up at the subsequent Committee meeting.

During the previous year there were no significant deficiencies found in internal financial controls that needed action by the Group Finance Director and the Melrose accounting function. Any control findings are followed up by the businesses to ensure a strengthening of the site-based accounting functions, including specific action plans to address the shortcomings identified. Follow-up visits were performed during 2020 which identified significant progress in the improvement of financial controls at sites.

A review of the internal audit process and scope of work covered by the internal auditor is the responsibility of the Committee, to ensure their objectives, level of authority and resources are appropriate for the nature of the businesses under review. This also considers the insights provided, improvements achieved and feedback from a number of sources including key representatives of the Company.

The Committee reviewed the reappointment of BM Howarth Ltd as internal auditor, following an assessment of the services delivered and approved their reappointment.

The Committee would like to thank the Group finance team, the internal auditor, the external auditor and the Company Secretariat for their hard work throughout 2020.

Liz Hewitt

Liz Hewitt
Chairman, Audit Committee
4 March 2021

Melrose Industries PLC Annual Report 2020

Nomination Committee report

The Nomination Committee (the "Committee") has overall responsibility for making recommendations to the Board on all new appointments and for ensuring that the Board and its Committees have the appropriate balance of skills, experience, independence, diversity and knowledge to enable them to discharge their respective duties and responsibilities effectively.

Archie G. Kane
Nomination Committee Chairman

Member	No. of meetings
Archie G. Kane (Chairman)	2/2
Justin Dowley	2/2
Liz Hewitt	2/2
David Lis	2/2
Charlotte Twyning	2/2
Funmi Adegoke	2/2

Discharge of responsibilities

The Committee discharges its responsibilities through:

- regularly reviewing the size, structure and composition of the Board including by means of overseeing the annual evaluation processes of the Board and its committees, and providing recommendations to the Board of any adjustments that may be necessary from time to time;
- giving full consideration to succession planning in order to ensure an optimum balance of executive and Non-executive Directors in terms of skills, experience and diversity, and in particular formulating plans for succession for the key roles of Chairman of the Board and Chief Executive;
- reviewing the career planning and talent management programme related to senior executives of the Company to ensure that it meets the needs of the business;
- managing the Board recruitment process and evaluating the skills, knowledge, diversity and experience of potential Board candidates in order to make appropriate nominations to the Board;
- reviewing and approving the diversity policy of the Company; and
- keeping up to date and fully informed on strategic issues and commercial changes affecting the Company and the markets in which it operates.

The Committee's terms of reference, which were last reviewed in November 2020, are available to view on the Company's website at: **https://www.melroseplc.net/about-us/governance/nomination-committee/**.

Committee membership and attendance

The Committee is made up 100% of independent Non-executive Directors and all of the current Non-executive Directors are members of the Committee.

The Committee is expected to meet not less than twice a year and during 2020, the Committee met twice. The attendance of its members at these Committee meetings is shown in the table above.

The Company Secretary acts as secretary to the Nomination Committee. On occasion, the Nomination Committee invites the Chief Executive, the executive Vice-Chairmen and the Group Finance Director to attend discussions where their input is required.

Board composition and succession planning

The Committee keeps under review the membership of the Board, including its size and composition, and makes recommendations to the Board on any adjustments it thinks necessary. The Committee recognises the value in attracting Board members from a diverse range of backgrounds who can contribute a wealth of knowledge, understanding and experience. The Committee works with the Board in order to ensure both of these matters are taken into account to aid effective succession planning.

During the year, Mr David Roper had intended on retiring from the Board. However, as a result of the global pandemic, the Board and Committee agreed that it was not the appropriate time to lose the expertise and experience of one of its co-founders. Mr Roper therefore agreed to delay his retirement and he will instead retire on 31 May 2021. We thank him for his long and successful service, particularly for the last twelve months, and wish him all the best.

Furthermore, as a result of the valuable contribution that Mr Peter Dilnot has made since joining Melrose as Chief Operating Officer in 2019, the Board in consultation with the Committee had approved the appointment of Mr Dilnot to the role of executive Director, and such appointment took effect on 1 January 2021. Mr Dilnot brings to the Board a deep understanding of the Melrose business model together with strong sector experience in engineering and aviation.

Succession planning arrangements for the Board as a whole were reviewed by the Committee in 2020. This included reviewing the skills set, tenure, diversity and independence of those already on the Board, and reviewing the Melrose senior management team including the career planning and talent management programmes in operation for them. In each case this was to allow the Committee to ensure that the right balance of skills, experience and diversity were reflected and being developed. Following such review, the Committee recommended to the Board that a new female Non-executive Director should be appointed, particularly with a view to further increasing diversity at Board level. Stonehaven International, an external recruitment consultancy firm unconnected with the Company and its Directors, has been retained to identify suitable candidates for the Board's consideration.

Given the strength of Melrose's decentralised operating structure in achieving the Group's strategic objectives, the Committee does not have direct involvement in the succession planning arrangements of the businesses. However, the Committee has access to the divisional executive teams through the business review cycle.

Chairman's tenure

The Committee also reviewed the role of Mr Justin Dowley as Melrose's inaugural Non-executive Chairman. Although Mr Dowley was appointed to the role in 2019, he first joined the Board as a Non-executive Director in September 2011, meaning he has served on the Board for over nine years. Under the UK Corporate Governance Code, this is a key date in the consideration of the independence of the Chairman.

In 2019 the Committee had recommended to the Board that Mr Dowley stay in his position for up to three years beyond 2020, subject to his annual re-election at the Company's AGM. This recommendation had been reached following a positive engagement process with key institutional shareholders on Mr Dowley's tenure.

During the year, the Committee remained supportive of its recommendation on Mr Dowley's tenure. Given the global pandemic, the acquisition of GKN, and the elevation of the Company to the FTSE 100, the Committee considered that there was a need for continuity and stability at Board level to facilitate succession planning arrangements and the development of a diverse Board. The Committee therefore considered it vital that any Chairman must have an in-depth understanding of the unique and particular drivers behind Melrose's business model so as to be able to provide the necessary leadership in such a period of change and uncertainty. Mr Dowley had also received strong support from shareholders at last year's AGM when shareholders approved his re-election to the Board.

Re-election of Directors

The effectiveness and commitment of each of the Directors is reviewed annually as part of the Board evaluation upon recommendations from the Committee. The Committee reviewed each Director in turn to satisfy itself as to the individual skills, relevant experience, contributions and time commitment of the Directors to the long-term sustainable success of the Company. The Committee and Board have satisfied themselves that each of the Directors should stand for re-election (and Mr Dilnot should stand for election for the first time), and the justifications for such re-elections (and election) are set out on pages 100 to 101 of this Annual Report and in the Notice of AGM on pages 208 to 213.

Diversity

Melrose is a meritocracy and individual performance is the key determinant in any appointment, irrespective of ethnicity, gender or other characteristic, trait or orientation. The Board and the Committee does however place great emphasis on ensuring that the membership of the Board and the pipeline for succession planning purposes reflects diversity. In particular, the past two Non-executive Director appointments have been women. Melrose has also achieved well ahead of schedule the Parker Review target of having one Director from an ethnic minority background on the Board by the end of 2021 following the appointment of Ms Funmi Adegoke to the Board in October 2019.

The Committee currently takes into account a variety of factors before recommending any new appointments to the Board, including relevant skills to perform the role, experience and knowledge needed to ensure a rounded Board and the benefits each candidate can bring to the overall Board composition. The Committee also takes into account race, ethnicity, country of origin, nationality, cultural background and gender in the selection process to ensure a diverse Board and it also strongly encourages executives to adopt the same approach when making appointments to the Melrose Executive Committee or the wider senior management team. The most important priority of the Committee, however, has been, and will continue to be, to ensure that the best candidate is selected, and this approach will remain in place going forward.

As at 31 December 2020 Melrose had 30% female representation on its Board. Melrose had been on track to achieve the Hampton-Alexander Review target of having 33% female representation on its Board by 2020 with the intended retirement of Mr Roper in May 2020. However, as a result of the global pandemic, the Board and Committee agreed that it was not the appropriate time to lose the expertise and experience of one of its co-founders. Mr Roper agreed to delay his retirement to assist the Company in navigating its way through the challenges presented by the pandemic. His knowledge and experience have been very helpful in ensuring that the businesses ended the year in a strong position. The Board's decision to delay Mr Roper's retirement was the reason that Melrose did not achieve the goal of 33% female Board members by the end of last year as had been intended. The middle of the crisis was not the time to lose someone of Mr Roper's experience, but this is now being addressed. Melrose is committed to achieving the Hampton-Alexander Review target in 2021 and along with Mr Roper's retirement it has started the process of recruiting for a new female Non-executive Director.

Below Board level, Melrose had established an Executive Committee in 2020 and focus has been placed on pursuing diversity at this level in order to pave the way for a diverse pipeline for succession planning purposes. This focus is represented through the fact that the Executive Committee and its direct reports consists of 34% female representation (and 35% female representation specifically at an Executive Committee level), which is in line with the Hampton-Alexander Review target of diversity at this level.

Further details of Melrose's commitment to diversity and the various diversity initiatives undertaken within the Group can be found in the Sustainability report on pages 78 to 85, and Melrose's diversity policy can be viewed on the Company's website at **www.melroseplc.net/sustainability/**. Additionally, further details on diversity and Board skills can be found on page 91 of this Annual Report.

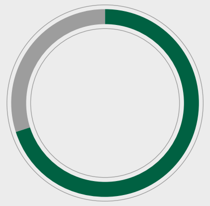
External evaluation

During 2020 an evaluation of the Chairman, the Board and its committees was undertaken in line with their respective terms of reference. These evaluations were conducted externally by Lintstock Ltd, a company unconnected with the Company and its Directors. The evaluation process involved direct engagement by Lintstock Ltd with each of the Directors. Lintstock Ltd prepared a report for the Board giving details of its evaluation and recommendations, and such report was subsequently discussed amongst the Board. The evaluation process demonstrated that the Board and its committees were operating effectively and the composition of such Boards and committees promoted the long-term sustainable success of the Company.

Archie G. Kane
Chairman, Nomination Committee
4 March 2021

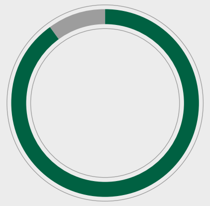
Diversity overview[1]

Board gender diversity



Male	70%
Female	30%

Board ethnic diversity



Non BAME[2]	90%
BAME[2]	10%

Melrose Executive Committee

Male	65%
Female	35%

Senior management and direct reports[3]

Male	66%
Female	34%

(1) As at 31 December 2020. Mr Dilnot joined the Board on 1 January 2021.
(2) Black, Asian and Minority Ethnic.
(3) In accordance with the UK Corporate Governance Code, senior management is defined as the executive committee, or the first layer of management below board level, including the Company Secretary.

Directors' Remuneration report

Chairman's Annual Statement

David Lis
Remuneration Committee Chairman

Dear Shareholders,

When I wrote to you this time last year, it was with the Group's 2019 preliminary results in mind, which had demonstrated another very successful year for Melrose in its "Buy, Improve, Sell" strategy. However, in the few short weeks following the announcement of the Group's 2019 preliminary results, the global situation had completely changed. The UK and much of the rest of the world had been placed into national lockdowns as a result of the COVID-19 pandemic, and we faced very difficult health and economic circumstances. The Board, along with the Melrose senior management team, took immediate action right across the Group to protect the health and wellbeing of our employees, customers and suppliers, and to ensure that our businesses dealt with the crisis in the best manner possible for all stakeholders.

The actions undertaken by the management team since the start of the crisis have been highly successful in addressing the significant immediate challenges presented by the pandemic, as well as positioning the Group to emerge from the crisis in the best shape possible. Although there remains plenty of hard work ahead, the focus has returned squarely on driving the strategic improvements that will generate returns in the future for our shareholders, in line with the Company's strategy.

We do not underestimate the enormity of the impact of the pandemic on the Group, but as a Board we remain cautiously optimistic, and we see some encouraging signs emerging in some of our businesses' end markets. Clearly the outlook for the aerospace sector remains difficult to predict with certainty, at least for so long as governments place widespread restrictions on travel.

We believe that the last twelve months have been a further demonstration of our resilient business model, and a management team with a proven track record. Your Board remains convinced that we will unlock the full potential of our businesses and continue to deliver the high level of returns that shareholders have enjoyed for many years.

Impact of COVID-19 on executive remuneration

As detailed elsewhere in this Annual Report, the pandemic had a significant impact on the Group's financial performance in 2020, which we expect will continue into 2021. We recognise the material impact on our shareholders too, including the withdrawal of dividends last year, which we are very pleased to be able to reinstate this year. All of the Group's businesses have been impacted by the pandemic, and the Melrose central team is no exception to this, including in respect of remuneration. One of the first actions that the Board took in March 2020 was to commit to a temporary 20% reduction in salary for the executive Directors and Melrose senior management team, as well as the basic fee for the Non-executive Directors, mirroring sacrifices made elsewhere in the Group.

Shortly afterwards in May, the 2017 Incentive Plan expired with no value payable to its participants, despite being on track to generate a reward before the impact of COVID-19 just over a month earlier. In a remuneration structure so heavily weighted to long-term incentive arrangements, this meant that for each of the three years of the 2017 Incentive Plan's performance period, the annual remuneration received by the executive Directors put them amongst the lowest paid management teams in the FTSE 100. The Committee did not seek to exercise its discretion to make any adjustment to this result. The management team is wholly aligned with shareholders and it has always been one of the central tenets of the Melrose remuneration structure that pay is only for performance.

The Company had also conducted a comprehensive engagement exercise during January and February 2020 as part of the preparation for the renewal of both the Directors' Remuneration Policy and the Company's long-term incentive arrangements. However, just prior to issuing last year's Notice of AGM, the world was plunged into crisis with the global outbreak of the COVID-19 pandemic. The speed and scale of the disruption caused by COVID-19 was unprecedented and, given the significant uncertainty, volatility and lack of clarity as to its impact on the Company's businesses and the wider economy, the Board determined that it was not appropriate for a resolution to be proposed at the 2020 AGM in relation to any long-term incentive arrangements. Instead, the 2020 Notice of AGM put forward the Directors' Remuneration Policy for approval in line with the successful consultation and stated that a new plan, continuing from the previous plan, would be separately put forward for shareholder approval at a later date when appropriate, incorporating any changes deemed necessary by the Board. The 2020 Employee Share Plan (see page 111) was eventually put to a shareholder vote in January 2021, and approved with strong support.

The impact of the pandemic on the Group's trading has also resulted in a substantial reduction in the annual bonuses awarded for 2020. With no reward available for audited diluted earnings per share growth, the basis for the 80% financial metric, opportunity for the executive Directors participating in the annual bonus scheme was limited to strategic factors only. Having fully considered management's performance during 2020 against the strategic factors, the Remuneration Committee has determined to make a full award for these, resulting in a bonus of 20% awarded for the year, as further detailed on page 114. This is the proper operation of the annual bonus scheme, without the exercise of any discretion by the Remuneration Committee, either upwards or downwards, which we did not consider appropriate. However, the award does not necessarily fully reflect the very hard work and success of the executive Directors over the last twelve months, for which we thank them.

Melrose continues to be a responsible steward of its businesses. The Committee notes that Melrose has fully repaid all payments received by the Group under the UK Coronavirus Job Retention Scheme during 2020. This means the performance of the business over the year has been delivered by the Company, without the assistance of UK Government support.

It is also worth noting that management are significant shareholders in the Company, together holding approximately 1.5% of the register as at 31 December 2020, putting them in the top 20 shareholders of the Company. Accordingly, they have shared the difficult experience during 2020 with their fellow shareholders.

2020 Employee Share Plan

As mentioned on page 110, an extensive consultation with shareholders had been carried out in early 2020 regarding the renewal of the Company's long-term incentive arrangements, prior to the proposal being withdrawn. While certain of the Group's businesses continued to feel the effects of the pandemic over a protracted period, and with the outlook for the aerospace sector remaining hard to predict with certainty, at least for so long as governments continued to place widespread restrictions on travel, the end markets of the rest of the Group continued to show encouraging signs. Considering how central the Melrose long-term incentive plan has always been to our success, in the fourth quarter of 2020, the Board felt it was appropriate to reinstate an amended plan following considerable shareholder engagement and to therefore suitably incentivise management to continue to drive exceptional shareholder value in the coming years. Shareholders made it clear throughout the year in the course of discussing with us that they shared this sense of urgency and wanted this addressed as soon as possible.

Following multiple rounds of engagement with our shareholders and other stakeholders (as described in further detail below), we were able to refine and simplify the proposal that was put to shareholders for approval at the end of 2020, followed by the general meeting to approve the 2020 Employee Share Plan in January 2021, which received strong support of 82.64%. The 2020 Employee Share Plan is a continuation of the highly successful long-term arrangement that has existed since Melrose was established in 2003, with added protections including the annual rolling cap. Full details can be found in the circular to shareholders dated 29 December 2020[1]. We thank shareholders for both their constructive engagement and ongoing support for the Company.

Melrose remuneration structure

Our long-standing executive remuneration structure is both well understood and well supported, being central to the success delivered for our shareholders, as evidenced by Melrose being the second highest performer of the FTSE 350 in terms of shareholder return over the decade to the end of 2019, a record that Melrose is keen to maintain in the years to come, as the COVID-19 crisis hopefully subsides.

We remain firm believers that Melrose's existing remuneration structure is entirely appropriate in supporting our "Buy, Improve, Sell" strategy. Our reward structure has always enjoyed strong support from our investors, including throughout the consultations during 2020, and as most recently demonstrated by the votes in favour of the Directors' Remuneration Policy at the 2020 AGM and the 2020 Employee Share Plan at the January 2021 general meeting.

Executive Directors' salaries continue to deliberately remain well below the lower quartile of our FTSE 100 peers, with annual bonuses similarly capped well below our peers at 100% of salary. With the increasing focus on sustainability, during 2021 the Committee will consider the best way to ensure this is properly incorporated into the Company's remuneration structure. The only benefits that executive Directors receive are medical cover and a pension contribution capped at 15% of salary, being the same percentage contribution that all Melrose employees receive, and lower than most FTSE 100 peers in the last year. The table on page 115 sets out the most recently available CEO annual remuneration (excluding the LTIP element for comparison) and puts this deliberate strategy in context, highlighting a difference of almost £2 million from the average FTSE 100 CEO annual remuneration in 2019.

As this and the table on page 115 clearly indicate, the opportunity for significant reward has always been heavily weighted to the Company's long-term incentive arrangements, which are long-term in nature and entirely based on performance. Executive Directors have the opportunity to share in the value they create for shareholders above a threshold return over a three-year performance period; however, if executive Directors do not deliver the required level of performance to achieve the threshold return, they receive no payout.

(1) Available at **www.melroseplc.net/media/2587/291220-melrose-circular.pdf**.

2020 clearly demonstrated the application of our remuneration strategy, with executive Directors receiving an inflationary-only increase to base salary of 3%, but with total remuneration decreasing by approximately 6%. In particular, no awards crystallised under the 2017 Incentive Plan, which had been on track to produce a reward for participants prior to the impact of COVID-19.

We strongly believe that our remuneration structure continues to be the right approach for Melrose. Under the 2020 Employee Share Plan recently approved by shareholders, executive Director awards are expected to continue to be made in shares and will be subject to a further two-year holding period, so that executive Directors remain completely aligned with shareholders. All other elements of remuneration continue to be pegged below or in line with the lower quartile of FTSE 100 peers. The Committee strongly believes that the 2020 Employee Share Plan will continue to be very effective in incentivising management to deliver real value to shareholders over the performance period.

Full details are set out in the Annual Report on Remuneration on pages 112 to 126 that will be put to an advisory vote at the 2021 AGM.

Stakeholder engagement

Melrose always strives for the full support of all its shareholders in all that we do. Our shareholders are critical to our success, we keep them informed, and their support is never taken for granted. Never is this more true than during challenging times like we experienced in 2020. As detailed in the Annual Report on Remuneration on page 113, we consulted extensively with shareholders and proxy advisors throughout the course of 2020 in relation to both the renewal of the Directors' Remuneration Policy at the 2020 AGM and the renewal of the Company's long-term incentive arrangements (including the related consequential amendments to the Directors' Remuneration Policy). Throughout multiple rounds of our engagement with shareholders, we received a significant level of helpful and constructive feedback from them, which assisted the Committee in shaping and refining the final proposals, and we sincerely thank our shareholders for their time.

Adjustments to the final proposals for both the Directors' Remuneration Policy and the 2020 Employee Share Plan (including the related consequential amendments to the Directors' Remuneration Policy) were made as a direct result of shareholder feedback, to incorporate further protections for shareholders. The result was a strongly supported proposal that stayed true to the Melrose remuneration model and strategy, which struck the right balance between setting stretching targets for management whilst nonetheless making them attainable and effective, and acknowledging the impact of COVID-19 on the financial performance of the Group's businesses.

We were pleased that the 2019 Directors' Remuneration Report, the Directors' Remuneration Policy and the 2020 Employee Share Plan all received strong shareholder support at the 2020 AGM and the general meeting in January 2021, receiving voting outcomes of 99.57%, 98.40% and 82.64% respectively.

Your Board considers that the Melrose remuneration structure is highly successful, appropriate for the value creation strategy, and is critical to the ongoing long-term performance of the Company. We encourage you to provide your support for the Annual Report on Remuneration at the 2021 AGM.

Yours sincerely

David Lis

David Lis
Chairman, Remuneration Committee
4 March 2021

Annual Report on Remuneration

On behalf of the Board, I am pleased to present our annual report on Director remuneration (the "Annual Report on Remuneration") at the end of what we see as a positive year for Melrose, given the circumstances.

In this section of the Directors' Remuneration report, we set out:

- the actual performance and executive remuneration outcomes for the 2020 financial year; and
- the application of the current Directors' remuneration policy (the "Directors' Remuneration Policy") to the 2020 financial year and how the Directors' Remuneration Policy was operated in 2020.

The Directors' Remuneration Policy was approved by shareholders at the AGM on 7 May 2020 with over 98% of votes cast in favour of the resolution, and subsequently amended on 21 January 2021 to include the 2020 Employee Share Plan. This level of support was also reflected in the approval of the 2020 Employee Share Plan, which was approved by shareholders on 21 January 2021 with over 82% of votes cast in favour of the proposal.

The full details of the Directors' Remuneration Policy can be found on pages 103 to 111 of the 2019 Annual Report[1] and the full details of the amendments can be found on pages 15 to 24 of the circular to shareholders dated 29 December 2020[2].

Key elements of the Annual Report on Remuneration and where to find them

Melrose's Remuneration Strategy

Since the Company was first established in 2003, the Remuneration Committee (the "Committee") has pursued a consistent remuneration strategy that closely aligns the executive Directors with the Company's shareholders, drives the Company's "Buy, Improve, Sell" model and has been central to its success. This strategy is based around four key principles – namely, that executive remuneration is:

(1) Simple – since Melrose was first established, executive Directors have received the same four simple elements as the rest of the Melrose employees – base salary, annual bonus, pension contribution (15% of salary, being the same percentage contribution for all Melrose employees) and medical benefits – as well as being eligible under a single and consistent long-term incentive plan based on a single value creation metric.

(2) Transparent – each year, there is full and detailed disclosure in the Directors' Remuneration report of each component of remuneration, including an explanation of the calculation of any variable element and the current value of any unvested award pursuant to the Melrose Employee Share Plan.

(3) Supports the delivery of the value creation strategy – with the fixed elements and the annual bonus cap being deliberately pegged well below the lower quartile of FTSE 100 peers, the opportunity for any significant reward is heavily weighted to the Melrose Employee Share Plan, which is entirely based on the creation of shareholder value.

(4) Pays only for performance – executive remuneration is heavily weighted to the Melrose Employee Share Plan, which pays nothing to participants unless the executive Directors deliver a threshold return to shareholders over a three-year period, and only pays a significant award if they materially outperform in the creation of shareholder value.

These four key principles are wholly aligned with the UK Corporate Governance Code (the "Code") factors of clarity, simplicity, risk, predictability, proportionality and alignment to culture, as set out on page 125. The Committee ensured that it took all of these elements into account when establishing the Directors' Remuneration Policy, as well as its application to executive Directors during the period.

Operation of the Directors' Remuneration Policy in 2020

2020 was a difficult year for most of the world's businesses due to the impact of the pandemic. However, as this Annual Report and financial statements demonstrates, the hard work of management during the year ensured that we have been able to deliver a good performance in the circumstances. Management are continuing to make progress on their improvement plans for the businesses, although many were slowed during the year as the Board tackled the rapidly changing circumstances presented by the pandemic. It is based on this performance, and in line with Melrose's remuneration philosophy of paying only for performance, that the Committee has taken its decisions in respect of executive Director remuneration arrangements for 2020 and 2021.

The Committee understands that shareholders expect executive remuneration to be aligned with the overall experience of the Company, its shareholders, employees and other stakeholders. The Committee is also mindful of the need to consider the impact of COVID-19 on executive remuneration. As is demonstrated elsewhere in this Directors' Remuneration report – in particular, Comparison to Peers (page 115), CEO Pay Ratio (page 120), and Wider workforce considerations (page 122), we believe that the remuneration structure operated by Melrose, and the outcomes produced by the operation of this structure, are appropriate and result in a strong alignment between the executive Directors, shareholders and other stakeholders.

(1) Available at **www.melroseplc.net/media/2536/melrose-ar2019.pdf**.
(2) Available at **www.melroseplc.net/media/2587/291220-melrose-circular.pdf**.

2020 key decisions

The Committee remains committed to a responsible approach to executive pay in accordance with the current Directors' Remuneration Policy, which was effective from the close of the 2020 AGM (as amended with effect from the close of the general meeting that took place on 21 January 2021), and its four key remuneration principles.

In line with increases in previous years, an inflationary increase of 3% was made to the executive Directors' base salaries with effect from 1 January 2020, consistent with the salary rises awarded to the wider Melrose head office population. Salaries remained below the lower quartile of the FTSE 100, as is demonstrated by the table on page 115. There were also inflationary increases made to Non-executive Director fees with effect from 1 January 2020, as set out on page 123. It is noted that all members of the Board, both executive and Non-executive Directors, took a temporary 20% reduction to their salary or fee in 2020 to support the wider Group in its cash management efforts as a result of the COVID-19 pandemic.

Following an extensive consultation with key shareholders and other stakeholders in January and February 2020, the Committee finalised its proposal for the renewal of the Directors' Remuneration Policy. It was as a direct result of this engagement that further protections for the benefit of shareholders were included, such as the increased minimum shareholding requirements for executive Directors of 300% of salary and post-cessation minimum shareholding requirements of 300% of salary for two years post-cessation. The Directors' Remuneration Policy was approved at the 2020 AGM with over 98% support.

Another key decision taken by the Committee in 2020, which is mentioned in my Annual Statement, was the decision not to propose a resolution for the renewal of the Company's long-term incentive arrangements at the 2020 AGM, due to the impact of COVID-19. This had followed a successful consultation with shareholders at the beginning of the year in relation to the renewal of both the Directors' Remuneration Policy and the long-term incentive arrangements, but as a Committee we felt that given the significant uncertainty, volatility and lack of clarity as to COVID-19's impact on the Company's businesses and the wider economy, it was not appropriate for a resolution to be proposed at the 2020 AGM in relation to any long-term incentive arrangements. Given how critical management incentivisation is to the Company's success, and with executive remuneration being heavily weighted towards the long-term incentive plan, this was not a decision that we took lightly.

We were pleased to see encouraging signs in the end markets of most of the Group's businesses by the fourth quarter of 2020. With this in mind, we returned to shareholders with a revised proposal for the 2020 Employee Share Plan, to reflect the impact of the pandemic on the Group. Following constructive feedback from shareholders, we incorporated further shareholder protections into the 2020 Employee Share Plan that was eventually put forward to shareholders for approval at the end of 2020, followed by the general meeting to approve the 2020 Employee Share Plan in January 2021. The Conditional Awards under the 2020 Employee Share Plan were granted on 29 December 2020, subject to approval by shareholders. The Committee is very pleased that the 2020 Employee Share Plan was approved by shareholders in January 2021 with over 82% support, reaffirming their belief in the Melrose remuneration structure.

Although the annual bonus outcomes for 2020 were finally determined by the Committee in 2021, we refer to them here for completeness, as they are a key decision relating to the reporting period. As mentioned in my Annual Statement, the financial element of the annual bonus was not met, due to the impact of the pandemic on the Company's financial performance. The Committee carefully considered the strategic objectives and the extent to which these were met during 2020. As is detailed further on page 116, the Committee felt that management's performance met the strategic objectives in full, without any basis for a deduction, and have therefore determined to make an award in this regard of the full 20%.

The Committee has reviewed the remuneration outcomes for the year and confirms that the Directors' Remuneration Policy operated as intended during the year and that there were no deviations from the Directors' Remuneration Policy during the year. The Committee felt that the incentive outcomes were in line with the overall performance of the Group and therefore did not exercise any discretion to alter the outcomes from the application of the performance conditions.

Stakeholder engagement

We constantly seek the views of our investors, which becomes particularly important at the time of remuneration renewals, as well as during times of heightened uncertainty. As mentioned in my Annual Statement last year, we conducted an extensive stakeholder engagement exercise during January and February 2020 as part of the preparation for the renewal of both the Directors' Remuneration Policy and the Company's long-term incentive arrangements. This engagement was constructive and helpful and included numerous discussions with proxy advisors and key shareholders holding in excess of 65% of our register. Feedback received during this initial engagement led to adjustments to the final proposals for the Directors' Remuneration Policy and long-term incentive arrangements that were approved by the Board to be put to shareholders at the AGM in 2020. The Committee was pleased that the 2019 Directors' Remuneration Report and the Directors' Remuneration Policy were approved by shareholders at the 2020 AGM with high rates of approval (with 99.57% and 98.40% voting in favour, respectively).

This engagement exercise had encompassed both the renewal of the Directors' Remuneration Policy and the renewal of the Company's long-term incentive arrangements. However, just prior to issuing the 2020 Notice of AGM, the Board took the decision to postpone the renewal of the long-term incentive arrangements given the significant uncertainty, volatility and lack of clarity resulting from the pandemic, to a more appropriate time.

With the publication of our half-year results in September 2020, and the positive messages and trends highlighted by those results, we felt that presented an appropriate time to return to shareholders with a revised proposal for the 2020 Employee Share Plan, which would be adjusted appropriately to reflect the impact of COVID-19 on the Group's financial performance. Over a three-month period with multiple rounds of consultation, we discussed the revised proposal with key shareholders representing over 75% of our register. Shareholders reconfirmed their belief in the Melrose remuneration structure and played a significant role in helping the Committee finalise the proposal for the 2020 Employee Share Plan. Over the course of the consultation, we made a number of adjustments to the proposal in line with shareholder feedback, to incorporate further shareholder protections, which resulted in the final proposal that was put to shareholders at the end of 2020. The Committee was pleased that the 2020 Employee Share Plan was approved by shareholders at the general meeting in January 2021, with 82.64% voting in favour.

This outcome reaffirmed the support of our shareholders for the Melrose remuneration structure, as well as reaffirming the belief that our shareholders have in the management team to deliver exceptional returns. It is clear that our key shareholders understand and appreciate that the Melrose remuneration structure is deliberately not the same as the standard FTSE company, a point that we note is encouraged by the UK Stewardship Code. However, it is appropriate for the Melrose model, as it properly incentivises management and drives the value creation strategy. The 2020 Employee Share Plan also, as a direct result of shareholder feedback, incorporates strong protections for shareholders against the risk of excessive pay and windfall gains, benchmarking both the 2020 Employee Share Plan and the Directors' Remuneration Policy very well against the Code and the guidelines of other stakeholders who have published their views on remuneration.

The Committee will continue to engage with stakeholders on matters relating to executive remuneration during the course of 2021, as appropriate.

Directors' Remuneration report
Continued

Business performance
Immediately prior to the global onset of the pandemic at the start of 2020, the Company was continuing its work to unlock the full potential of the Group's businesses, having recently announced a very successful set of 2019 preliminary results. As the pandemic hit the Group, management's focus was forced to quickly turn to more immediate actions such as prioritising strong cash management, quickly implementing operational initiatives to generate efficiency improvements, and carefully executing restructuring projects to significantly improve the Group's trading performance in 2021 and beyond. 2020 was therefore a challenging year for Melrose, as demonstrated by these results. However, we are already beginning to see the benefits of these decisive management actions and we are looking forward in 2021 to repositioning the businesses on the same improvement tracks that they were on prior to the pandemic.

We have seen some encouraging signs of recovery in the end markets of some of our businesses, including the GKN Automotive, GKN Powder Metallurgy and Nortek Air Management divisions. The aerospace sector continues to be challenging and neither we, nor the market, expect this to change for some time. However, the Melrose business model has proven resilient through varied economic cycles and previous crises, and our management team have a proven track record in delivering exceptional returns for shareholders, even in times of crisis. We therefore remain cautiously optimistic as to 2021 performance.

This Annual Report and financial statements and specifically the Group's strategic KPIs on pages 34 to 35 demonstrates the good progress that was made in 2020 towards the achievement of our objective of building better, stronger businesses under our ownership, even against the backdrop of the pandemic. The Company's Annual Bonus Plan focuses directly and indirectly on rewarding executive Directors and Melrose senior management for delivering these KPIs. The 2020 Employee Share Plan is designed to reward the flow-through of the successful implementation of the strategy into longer-term sustainable shareholder returns, consistent with previous incentive plans.

Sustainability
We appreciate and understand that investors are requiring enhanced disclosure from issuers around matters relating to sustainability. It was with this in mind that management produced the Company's inaugural ESG report, included in last year's Annual Report and financial statements, and significant work has gone into enhancing our disclosures for 2020, as contained in the Sustainability report on pages 58 to 87. As the Sustainability report demonstrates, there is a lot of excellent work being done by our businesses to develop cutting-edge technology and products that help them and their customers to deliver on their environmental goals.

The Committee considers that the most appropriate place to recognise performance in relation to sustainability within the remuneration structure is in the Annual Bonus Plan, as it allows for performance assessment against a number of strategic elements, in addition to the focus on financial elements. In order to better align the strategic elements with the focus and importance placed on sustainability matters, during 2021, the Committee will be considering how progress on sustainability matters may be better incorporated into the executive remuneration structure. To the extent that changes proposed as a result of this review require an amendment to the Directors' Remuneration Policy, we will consult with key shareholders and their approval for any amendments will of course be sought.

Single total figure of remuneration for the executive Directors for the 2020 financial year (audited)
The following chart summarises the single figure of remuneration for 2020 in comparison with 2019[1]:

Executive Director	Period	Total salary and fees[2] £000	Taxable benefits £000	Bonus £000	LTIP[3] £000	Pension[4] £000	Total Fixed £000	Total Variable £000	Total £000
Christopher Miller	2020	490	2	n/a	0	80	**572**	**0**	**572**
	2019	520	3	n/a	–	78	**601**	**0**	**601**
David Roper	2020	490	3	n/a	0	80	**574**	**0**	**573**
	2019	520	4	n/a	–	78	**602**	**0**	**602**
Simon Peckham	2020	490	3	107	0	80	**573**	**107**	**680**
	2019	520	3	375	–	78	**601**	**375**	**976**
Geoffrey Martin	2020	395	10	86	0	65	**470**	**86**	**556**
	2019	419	10	302	–	63	**492**	**302**	**794**
Total	**2020**	**1,866**	**18**	**193**	**0**	**305**	**2,189**	**193**	**2,382**
	2019	**1,979**	**20**	**677**	**–**	**297**	**2,296**	**677**	**2,973**

(1) The "Total" figures in the above table may not add up to the sum of the component parts due to rounding.
(2) The executive Directors, with the rest of the Board, committed to a temporary 20% reduction in salary in 2020 to support the Company's cash management strategy in light of the pandemic. The amounts stated in the table for 2020 are the actual amounts that were paid to the executive Directors.
(3) The 2017 Incentive Plan crystallised on 31 May 2020 for no value. The 2020 Employee Share Plan, which has a commencement date of 31 May 2020, is a five-year plan in total (comprised of a three-year performance period and a two-year holding period). Accordingly, no value was vested to participants in respect of the year to 31 December 2020 under either plan.
(4) All amounts attributable to pension contributions were paid as a supplement to base salary in lieu of pension arrangements.

Comparison to Peers
The total remuneration of £680,113 paid to the Melrose Chief Executive in respect of 2020 was approximately 30% lower than last year's total, due to the temporary 20% salary reduction and significantly reduced annual bonus award, as detailed below. The Committee benchmarked the Melrose Chief Executive's 2020 pay against the most recent available remuneration information from our FTSE 100 peers (being 2019)[1].

As the table below shows, the single total figure of remuneration for the Melrose Chief Executive in 2020 was well below the lower quartile of FTSE 100 peers, and less than one third of, or almost £2 million less than, the FTSE 100 average. This demonstrates in practice the Committee's policy of deliberately setting salary, benefits and annual bonus for the executive Directors low, with the opportunity for significant reward being heavily weighted towards the Melrose Employee Share Plan, which is entirely performance based and ensures that executive Directors only receive substantial rewards when they have outperformed and created very significant value for shareholders.

Metric (GBP '000)	Melrose Chief Executive	FTSE 100 Lower Quartile	FTSE 100 Average	FTSE 100 Upper Quartile
Total	680	1,653	2,410	2,981

Each of the elements in the single figure table is set out in more detail below, along with the benchmark for the Melrose Chief Executive to the most recent available information for our FTSE 100 peers (being 2019).

Base Salary
Salaries are fixed at a level which is well below the lower quartile of FTSE 100 peers. Each executive Director received an inflationary increase in base salary of 3% effective from 1 January 2020, although base salaries were subject to a temporary 20% reduction during the year to support the Company's cash management strategy in light of the pandemic.

Metric (GBP '000)	Melrose Chief Executive	FTSE 100 Lower Quartile	FTSE 100 Average	FTSE 100 Upper Quartile
Annual Salary	490	700	944	1,100

Pensions
Executive Directors receive the same 15% of base salary pension contribution[2] as the rest of the Melrose employees, which the Committee notes is in line with the lower quartile of pension contributions in the FTSE 100 and is also within the range of the wider workforce contributions in the UK. This contribution rate has not changed since Melrose was founded and no executive Director participates or has ever participated in a Group defined benefit or final salary pension scheme.

Metric (GBP '000)	Melrose Chief Executive	FTSE 100 Lower Quartile	FTSE 100 Average	FTSE 100 Upper Quartile
Pension Contribution	80	124	217	289
Pension Contribution %	15%	15%	21%	25%

Benefits
Executive Directors receive the same taxable non-pension benefits as the rest of the Melrose employees, being generally private medical insurance and a fuel allowance. The Group Finance Director also received paid train travel to and from London.

Metric (GBP '000)	Melrose Chief Executive	FTSE 100 Lower Quartile	FTSE 100 Average	FTSE 100 Upper Quartile
Benefits	3	20	65	69

Annual Bonus
Annual bonuses are entirely performance driven and are calculated by the Committee using two elements: 80% being based on audited diluted earnings per share growth; and 20% based on the achievement of strategic elements. The maximum bonus opportunity is set at 100% of base salary, which is significantly below the lower quartile maximum annual bonus opportunity for other FTSE 100 companies as set out in the table below. Neither of the executive Vice-Chairmen participate in the annual bonus scheme.

Metric (GBP '000)	Melrose Chief Executive	FTSE 100 Lower Quartile	FTSE 100 Average	FTSE 100 Upper Quartile
Annual Bonus	107	662	1,188	1,600
Max bonus opportunity %	100%	150%	202%	215%

(1) For comparison purposes, the included peer information excludes any payments made under long-term incentive arrangements, as none were payable to the Chief Executive in 2020.
(2) All of the amounts attributable to pension contributions were paid as supplements to base salary in lieu of pension arrangements.

Directors' Remuneration report

Continued

2020 Annual Bonus (audited)

The 2020 Annual Bonus has applied a consistent approach to previous years, in line with the current Directors' Remuneration Policy. The Committee awarded participating executive Directors a bonus of 20% of their 2020 unadjusted base salary, based on 2020 performance, with the full breakdown of the award calculation set out below.

As is shown by the table, the financial element of the 2020 Annual Bonus was not satisfied and therefore no award was made for this part of it. The Committee did not seek to exercise any discretion to adjust for this or to adjust the performance conditions in any way to account for the impact of COVID-19. With respect to the strategic element, the Committee determined that each of the strategic objectives were fully met during 2020 and therefore that the strategic element was met in full. The Committee determined that no exercise of discretion to adjust this element of the award was required. Full disclosure of the strategic objectives and why the Committee determined that these had been met is provided below.

In addition to a detailed and thorough consideration of each of the strategic objectives and management's performance against them during 2020, the Committee was also mindful of the guidance published by the Investment Association regarding the payment of executive annual bonuses during the COVID-19 pandemic. In particular, the Committee felt that the Company's proposal to reinstate the payment of dividends to shareholders in 2021, the repayment by the Company of all payments received by the Group under the UK Coronavirus Job Retention Scheme during 2020, and the Company choosing not to raise additional capital from shareholders during the period, meant that the executive remuneration awarded for 2020 is appropriate and in line with that guidance, and that no exercise of discretion to adjust the strategic element of the award for the impact of COVID-19 was required.

Financial Objectives (80%)					Percentage of maximum bonus earned
	Threshold	**Target**	**Maximum**	**Actual Performance**	
EPS Growth	**5%**	**10%**	**20%**	**0%**	
% award	20%	40%	80%	0%	
EPS Growth sub-total:					**0%**

Strategic Objectives (20%)		Percentage of maximum bonus earned
Cash generation across the Group – maximum 4%	This is always a key objective for the Group, particularly so during 2020, with its businesses being in the "Improve" phase of the Company's "Buy, Improve, Sell" strategy, and as a result of the pandemic. As demonstrated by these results, Melrose was able to end the year having generated adjusted free cash of £628 million, notwithstanding the challenges presented by the pandemic. This was a 6% increase on the previous year, reducing net debt to £2.85 billion and holding leverage to 4.1x adjusted EBITDA, despite reduced profit. This was well beyond the Board's expectations.	4%
Improvement in working capital – maximum 4%	Management continued to focus on working capital improvements and efficiencies in each of the divisions, particularly in the GKN businesses. Management were intensely focused on cash generation following the outbreak of the pandemic, as mentioned above. Consequently, management implemented increased discipline in working capital management practices across the Group, based on strict inventory control and backed by forensic weekly cash management calls with each business, and focused on working with the businesses to reduce and align working capital with reduced sales. As a result, net working capital for the year reduced by £424 million, a reduction of 52% on the previous year.	4%
Resolution of GKN onerous contract burden – maximum 4%	Significant improvements continued to be made on the GKN onerous contracts during 2020. With management's full support, all of the GKN businesses continued to take significant steps to resolve a number of their key onerous contracts, with over 60% of the total original exposure under these contracts having now been resolved. This is a significant step forward in management's aim to eradicate the entire exposure in the coming years, as part of its wider improvement strategy for the GKN businesses.	4%
Intensification of acceleration of sustainability performance and reporting – maximum 4%	As demonstrated by the 2020 Sustainability report, management have significantly improved the level of disclosure on sustainability matters, as well as continuing to invest in sustainable products and processes. The Group also committed to net zero greenhouse gas emissions by 2050 and is actively pursuing the development of critical zero-emissions technology in order to help decarbonise the aerospace and automotive sectors. At the same time, there has been a reduction in emissions from production across the Group, including an 11% year-on-year reduction in greenhouse gas emissions. The cumulative effect of these actions is expected to translate into much improved ratings when the relevant agencies reassess the Group's sustainability score later this year.	4%
Restructuring projects and divestment of non-core businesses – maximum 4%	Management have continued to work with each of the businesses to assess the need for restructuring programmes, a number of which intensified as a result of the pandemic's impact on the end markets of the businesses and their customers. The strong cash generation of the Group enabled management to undertake the necessary restructuring programmes in GKN in 2020 that will deliver over £125 million full year benefit for 2021, as discussed further in the Chief Executive's review on page 12. Management has also continued to assess the Group's businesses and to strategically review potential divestments for non-core assets, including the disposal of the GKN Wheels & Structures business, which successfully signed and completed during the period.	4%
Strategic Objectives sub-total:		**20%**
Total annual bonus for 2020:		**20%**

All bonus payments for 2020 will be made in cash, as both participating executive Directors have exceeded their minimum shareholding requirements. See page 118 for details of the requirements.

Long-term incentive arrangements (audited)

2017 Incentive Plan

Following the withdrawal of the proposal for the renewal of the Company's long-term incentive arrangements, the 2017 Incentive Plan expired in May 2020 with no value payable to its participants, despite being on track to generate a reward before the impact of COVID-19. The Committee did not seek to adjust this outcome on the crystallisation date of the 2017 Incentive Plan or to adjust the performance conditions, whether for share price appreciation, the impact of COVID-19, or otherwise.

Long-term incentive arrangements granted in the year

The 2020 Employee Share Plan, which was approved by shareholders on 21 January 2021, is due to crystallise on 31 May 2023. On expiry, therefore, it will be the only Melrose long-term incentive plan for a six-year period. Participants in the 2020 Employee Share Plan share in 7.5% of the increase in invested capital above a 5% annual charge, measured at the end of a three-year performance period commencing on 31 May 2020. The Committee still considers that this is the appropriate performance condition in light of the Company's business model and strategy. Awards are subject to an annual rolling cap and downwards adjustment in the event of an earlier than expected aerospace market recovery, which means that executive Directors will not be rewarded for windfall gains. The preference expressed by most shareholders involved in our consultation was for such a market adjustment to be included, rather than for the performance period to be adjusted or delayed. The awards under the 2020 Employee Share Plan are structured as Conditional Awards, which are contingent rights to be granted an award of ordinary shares of the Company or a nil cost option (exercisable into ordinary shares of the Company) on the crystallisation date.

As set out in the circular dated 29 December 2020[1], which contains full details of the 2020 Employee Share Plan, Conditional Awards have been granted to the executive Directors as set out in the table below, with the remainder being allocated to other members of the Melrose senior management team. The Conditional Awards of the executive Directors under the 2020 Employee Share Plan were made in one grant on 29 December 2020, subject to approval by shareholders. This approval was granted at the general meeting that was held on 21 January 2021.

Executive Directors	Position	Participation Rate Percentage
Christopher Miller	Executive Vice-Chairman	14%
David Roper[1]	Executive Vice-Chairman	5%
Simon Peckham	Chief Executive	16%
Geoffrey Martin	Group Finance Director	16%
Peter Dilnot[2]	Chief Operating Officer	12%

(1) David Roper will retire at the end of May 2021.
(2) Peter Dilnot was appointed as an executive Director of the Company with effect from 1 January 2021.

The three-year performance period of the 2020 Employee Share Plan commenced on 31 May 2020 and will not mature until the crystallisation date on 31 May 2023. As noted in the circular to shareholders dated 29 December 2020[1], the start price under the 2020 Employee Share Plan is 170 pence, assuming a crystallisation date of 31 May 2023. To provide an illustration of the current status of the 2020 Employee Share Plan, we note that the average price of an ordinary share for the 40 business days prior to 31 December 2020 was 161 pence, which is less than the start price of 170 pence. To be clear, no value can be received by participants until the crystallisation date, and so we include this information for illustrative purposes only.

We will continue to provide disclosure on the current performance of the 2020 Employee Share Plan in subsequent Directors' Remuneration reports during the remainder of the performance period.

Therefore no long-term incentives crystallised during the 2020 financial year under either the 2017 Incentive Plan or the 2020 Employee Share Plan, nor were any performance conditions adjusted to account for the impact of COVID-19.

Illustration and application of the Directors' Remuneration Policy in 2020

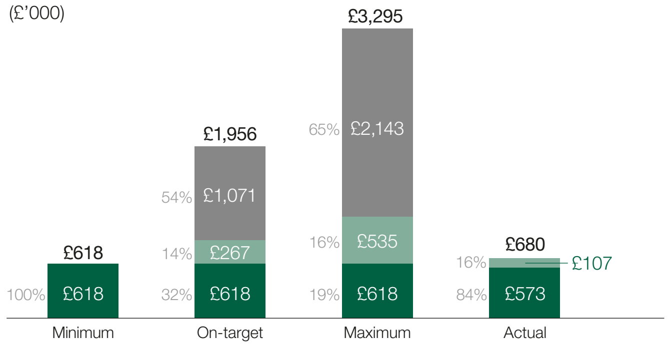
The charts set out below are updated versions of charts which appeared in the Directors' Remuneration Policy approved at the 2020 AGM. These set out an illustration of the current Directors' Remuneration Policy compared to the actual executive Director remuneration paid in 2020[1].

The executive Directors' options under the 2017 Incentive Plan could have delivered to them part of the growth in value of the Company from May 2017 to May 2020 (or an earlier trigger date determined in accordance with the Articles of Association). Accordingly, the value of participation in the 2017 Incentive Plan was not expressed as a multiple of salary but on a valuation done at the time of the renewal of the incentive plan in May 2017 (see circular dated 7 April 2017[2]). The 2017 Incentive Plan crystallised on 31 May 2020 with no value accruing to the scheme, and so the 2017 Incentive Plan expired with no award being made to participants.

The executive Directors' options under the 2017 Incentive Plan, in addition to any Incentive Shares (2017) held by the executive Directors, crystallised in May 2020 with no value payable to them, as the performance conditions had not been met.

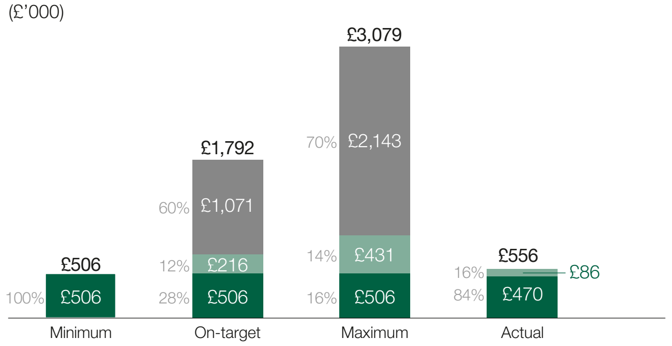
Simon Peckham

(£'000)



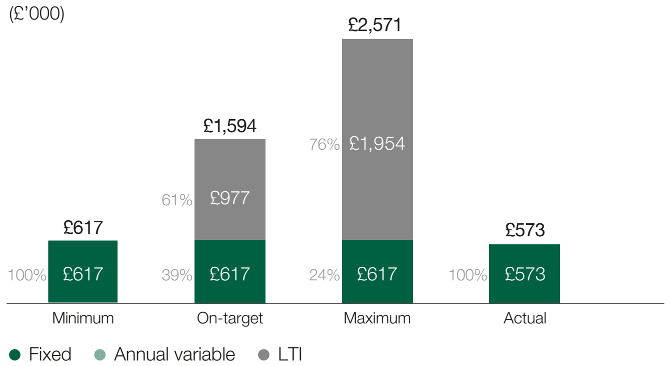
Geoffrey Martin

(£'000)



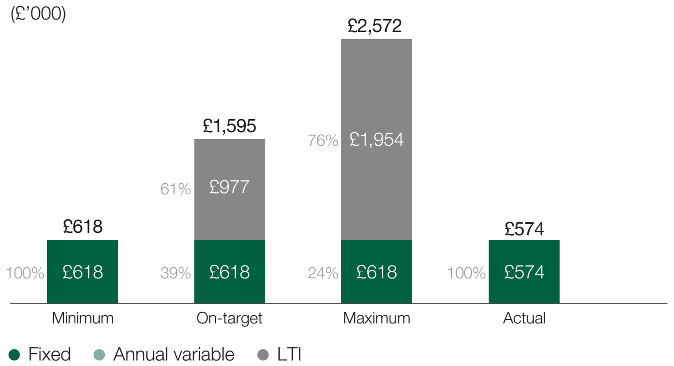
Christopher Miller

(£'000)



David Roper

(£'000)



In illustrating the potential reward under the Directors' Remuneration Policy compared to the actual single figures awarded for 2020, the following assumptions have been made:

- **Minimum performance:** fixed elements of remuneration only. Base salary effective from 1 January 2020, and benefits and pension rate as set out in the single figure table for the year ended 31 December 2020 on page 114.
- **On-Target:** fixed elements of remuneration as above, plus a bonus of 50% of salary (other than in the case of Christopher Miller and David Roper, who do not participate in the annual bonus arrangements), plus an amount in relation to the executive Directors' entitlements under the 2017 Incentive Plan, being 50% of the fair value of the award, calculated as set out above.
- **High-performance:** fixed elements of remuneration as above, plus a bonus of 100% of salary (other than in the case of Christopher Miller and David Roper, who do not participate in the annual bonus arrangements), plus an amount in relation to the executive Directors' entitlements under the 2017 Incentive Plan, being 100% of the fair value of the award, calculated as set out above.

(1) The total figures shown in the above bar charts may not add up to the sum of the component parts due to rounding.
(2) Available at **www.melroseplc.net/media/2587/291220-melrose-circular.pdf**.

Directors' Remuneration report

Continued

Minimum shareholding requirements and equity exposure of the Board (audited)

Executive Directors are subject to two concurrent minimum shareholding requirements. The first is to always hold at least an amount of shares equal to 300% of salary. The second requirement is for executive Directors to hold all of the shares acquired pursuant to the crystallisation of the 2017 Incentive Plan, after satisfying tax obligations following the crystallisation of that plan and subject to capital adjustments, and for a two-year holding period. As the 2017 Incentive Plan expired for no value on crystallisation in May 2020, there are no shares to which this requirement applies. A similar shareholding requirement applies in respect of the 2020 Employee Share Plan, which (to the extent that crystallisation results in an award of ordinary shares being made) will require executive Directors to hold all the shares they acquire pursuant to crystallisation of the 2020 Employee Share Plan, after satisfying tax obligations following the crystallisation of that plan and subject to capital adjustments, for the two-year holding period.

In the event that an executive Director were to leave the Company, he would be subject to a post-cessation minimum shareholding requirement of 300% of salary, for a two-year period following the date of cessation. This obligation is enforceable under direct contractual arrangements between the Company and each executive Director. In practice, this obligation has never been applicable as there have been no departures from the executive team since Melrose's formation in 2003 to date. However, we note that co-founder and Executive Vice-Chairman David Roper is due to retire on 31 May 2021, and these post-cessation obligations will apply to him from that date.

In reality, the executive Directors hold well in excess of these minimum amounts, which reflects their long-term stewardship of the Company and long-term investment in the Company's shares. It is the Committee's view that it is important when considering the remuneration paid in the year under the single figure to take a holistic view of how each executive Director's total wealth is linked to the performance of the Company. In the Committee's opinion, the impact on the total wealth of the executive Director is as important as the single figure in any one year; this approach encourages executive Directors to take a long-term view of the sustainable performance of the Company and aligns them with shareholders.

This is demonstrated by the following table, which sets out all subsisting interests in the equity of the Company held by the executive Directors as at 31 December 2020, as well as an indication as to the size of these interests relative to the entire issued share capital of the Company. It also sets out the number of ordinary shares of the Company held by each executive Director at the end of the 2019 and 2020 financial years and the impact on the value of these ordinary shares taking the closing mid-market prices for those dates:

Executive Directors(1)(2)	Applicable shareholding requirement (% salary)(3)	Current shareholding (% salary)(4)	Shareholding requirement met?	Shareholding (% ordinary share capital) as at 31 December 2020	Shares beneficially held on 31 December 2019(5)	Shares beneficially held on 31 December 2020(5)	Value of shares on 31 December 2019(6)	Value of shares on 31 December 2020(4)	Difference in value of shares between 31 December 2019 and 31 December 2020 £
Christopher Miller	300%	9,846%	Yes	0.55%	27,108,510	27,108,510	£65,087,533	£48,266,702	(16,820,830)
David Roper	300%	5,853%	Yes	0.33%	16,373,732	16,115,302	£39,313,331	£28,693,295	(10,620,035)
Simon Peckham	300%	6,324%	Yes	0.36%	17,265,565	17,413,217	£41,454,622	£31,004,233	(10,450,389)
Geoffrey Martin	300%	3,332%	Yes	0.15%	7,395,256	7,395,256	£17,756,001	£13,167,253	(4,588,756)

(1) Peter Dilnot is not included in the above table as he was appointed as an executive Director with effect from 1 January 2021.
(2) In addition to the share interests set out in the table, each of the executive Directors has an additional exposure by virtue of their Conditional Awards under the 2020 Employee Share Plan (see "Long-term incentive arrangements" on pages 16 and 17).
(3) The shareholding requirement under the current Directors' Remuneration Policy is 300% of base salary.
(4) For these purposes, the value of a share is 178.05 pence, being the closing mid-market price on 31 December 2020, being the last business day of the 2020 financial year.
(5) For these purposes, the interests of each executive Director listed in the table include any ordinary shares held by a person closely associated with that executive Director within the meaning of the EU Market Abuse Regulation, as it forms part of retained EU law by virtue of the European Union (Withdrawal) Act 2018.
(6) For these purposes, the value of a share is 240.1 pence, being the closing mid-market price on 31 December 2019, being the last business day of the 2019 financial year.

No executive Director may dispose of any ordinary shares without the consent of the Chairman of the Committee, which will not normally be withheld provided the executive Director will continue to hold at least the "minimum number" of ordinary shares referred to in the table above following any such disposal.

Between them, the executive Directors in 2020 purchased a further 689,222 ordinary shares in the Company and none were sold. David Roper gifted 800,000 ordinary shares during the period to family members for nil consideration, as part of standard family financial planning. There have been no changes in the ordinary shareholdings of the executive Directors between 31 December 2020 and 4 March 2021.

Please see page 123 for a table setting out the equity interests of the Non-executive Directors as at 31 December 2020.

(1) Available at **www.melroseplc.net/media/1728/21347274-_-1-_circular.pdf**.

Key decisions and statement of implementation for 2021

Salary review

The executive Directors in the period have received an inflationary increase of 3% to their base salaries with effect from 1 January 2021, consistent with the wider Melrose head office population, with the exception of the Group Finance Director, who received an additional 1% increase. The executive Directors' salaries for 2021 are therefore as follows:

Executive Director	Position	Salary with effect from 1 January 2021 £000
Christopher Miller	Executive Vice-Chairman	551
David Roper	Executive Vice-Chairman	551
Simon Peckham	Chief Executive	551
Geoffrey Martin	Group Finance Director	450
Peter Dilnot	Chief Operating Officer	450

Peter Dilnot was appointed as an executive Director with effect from 1 January 2021, having served as the Company's Chief Operating Officer since April 2019. His remuneration package is in line with the recruitment remuneration policy outlined in the Directors' Remuneration Policy. He will be included in the Annual Bonus Plan for 2021, along with the Chief Executive and Group Finance Director, and will therefore be eligible to receive an annual bonus in respect of the financial year ending 31 December 2021. As disclosed elsewhere in this report, Peter Dilnot is a participant in the 2020 Employee Share Plan. He will also receive the same benefits as the other executive Directors, including a pension contribution of 15% of salary. Full details of Mr Dilnot's executive remuneration in respect of the 2021 financial year will be disclosed in next year's Directors' Remuneration report.

Non-executive Directors' basic fees for 2021 have also been increased by 3%, with effect from 1 January 2021, which is consistent with the increase for the executive Directors and in line with FTSE 100 peers.

Pensions and benefits

For 2021, standard benefits will be provided to the executive Directors in line with the Directors' Remuneration Policy and the pension contribution rate remains at 15% of salary, the same percentage contribution rate as for all Melrose employees.

Annual bonus

The overall framework for the executive Director annual bonus arrangements for 2021 will remain the same as in 2020, with a maximum bonus opportunity of 100% of salary, based on financial and strategic performance metrics. The financial performance metrics remain as set out in the Directors' Remuneration Policy. The Committee considers that the strategic performance measures are commercially sensitive but will disclose the nature of those measures on a retrospective basis, where appropriate, on a similar basis to the disclosure on page 116 in respect of the annual bonus for the year ending 31 December 2020. In addition, as described on page 114, the Committee will commence a review on how to better incorporate progress on sustainability matters into the Company's executive remuneration structure, with any changes proposed as a result of this review being put to shareholders for their approval next year, to the extent required.

Long-term incentive arrangements

Given the nature of the long-term incentive arrangements that the Company has in place (see "Long-term incentive arrangements" on pages 16 and 17, no grants will be made to the executive Directors during 2021.

Regulatory disclosures

Chief Executive remuneration for previous ten years

In accordance with the regulations governing the reporting of executive Director remuneration, the total figure of remuneration set out in the table below includes the value of long-term incentives vesting in respect of the relevant financial year. This means that the full value of the crystallisation of the 2009 Incentive Plan on 11 April 2012 is shown for the year ended 31 December 2012 and that the full value of the 2012 Incentive Plan which crystallised in May 2017 is shown for the year ended 31 December 2017, although these each represent rewards earned over the previous five years. As disclosed in detail on pages 110 and 116, the 2017 Incentive Plan crystallised in May 2020 for no value. The next award in relation to long-term incentive arrangements is therefore not payable until May 2023, and only if the performance conditions are met.

Financial year	Chief Executive	Non-LTIP £	LTIP £	Total remuneration £	Annual bonus as a percentage of maximum opportunity	Long-term incentives as a percentage of maximum opportunity
Year ended 31 December 2020	Simon Peckham	680,113	0(1)	680,113	20%	n/a(2)
Year ended 31 December 2019	Simon Peckham	976,000	0	976,000	72%	–
Year ended 31 December 2018	Simon Peckham	1,049,000	0	1,049,000	95%	–
Year ended 31 December 2017	Simon Peckham	994,000	41,770,000(3)	42,764,000	90%	n/a(4)
Year ended 31 December 2016	Simon Peckham	987,725	0	987,725	95%	–
Year ended 31 December 2015	Simon Peckham	928,541	0	928,541	88%	–
Year ended 31 December 2014	Simon Peckham	773,167	0	773,167	58%	–
Year ended 31 December 2013	Simon Peckham	927,276	0	927,276	100%	–
Year ended 31 December 2012(5)	Simon Peckham	489,372	19,791,212	20,280,584(6)	64%	n/a(7)
	David Roper	259,040	10,656,806	10,915,846(6)	64%	n/a(7)
Year ended 31 December 2011	David Roper	811,152	0	811,152	84%	–

(1) As disclosed in detail on pages 110 and 116, the 2017 Incentive Plan crystallised in May 2020 for no value.
(2) Although the 2017 Incentive Plan crystallised in May 2020 for no value, because the value that would have been derived on the crystallisation of the Incentive Shares (2017) and options depended upon the shareholder value created over the relevant period, it would not have been possible to express the value derived as a percentage of the maximum opportunity.
(3) The value derived in 2017 from the 2012 Incentive Shares represents the Chief Executive's share, determined in accordance with the terms of those shares, of the shareholder value created over a period of approximately five years. This amount was paid in shares, not cash.
(4) On the crystallisation in May 2017 of the 2012 Incentive Plan, participants as a whole were entitled to 7.5% of the increase in shareholder value from 22 March 2012 to 31 May 2017. Because the value derived on the crystallisation of the Incentive Shares (2012) depended upon the shareholder value created over the relevant period, it is not possible to express the value derived as a percentage of the maximum opportunity.
(5) In the year ending 31 December 2012, David Roper was Chief Executive for the period from 1 January 2012 until 9 May 2012 and Simon Peckham was Chief Executive for the period from 9 May 2012 onwards. In the table above, the "Total remuneration" figure shows, in respect of David Roper, his total remuneration in respect of his service in the period from 1 January 2012 to 9 May 2012 and in respect of Simon Peckham, his total remuneration in respect of his service in the period from 9 May 2012 to 31 December 2012. Included in this figure for each of David Roper and Simon Peckham is the value of the long-term incentives vesting in the year, pro-rated to reflect the portion of the year for which he was Chief Executive.
(6) The value derived in 2012 from the 2009 Incentive Shares represents the relevant Chief Executive's share, determined in accordance with the terms of those shares, of the shareholder value created over a period of approximately five years.
(7) On the crystallisation in April 2012 of the 2009 Incentive Plan awarded in 2009, participants as a whole were entitled to 10% of the increase in shareholder value from 18 July 2007 to 23 March 2012. Because the value derived on the crystallisation of the 2009 Incentive Shares depended upon the shareholder value created over the relevant period, it is not possible to express the value derived as a percentage of the maximum opportunity. The crystallisation of the 2009 Incentive Shares was satisfied by the conversion of those shares into ordinary shares.

Directors' Remuneration report
Continued

CEO Pay Ratio
Our median CEO to employee pay ratio for 2020 continued to be low at 16:1. The following table provides pay ratio data in respect of the Chief Executive's total remuneration compared to the 25th, median and 75th percentile UK employees.

Financial year	Method	25th percentile pay ratio	Median pay ratio	75th percentile pay ratio
Year ended 31 December 2020	Option A	20:1	16:1	13:1
Year ended 31 December 2019	Option A	30:1	24:1	19:1

The employees used for the purposes of the table above were those employed by any business within the Group on 31 December 2020 and the remuneration figures were determined with reference to the financial year to 31 December 2020. Option A was chosen as it is considered to be the most accurate way of identifying the relevant employees. This captures all relevant pay and benefits and aligns to how the single figure table is calculated for the Chief Executive and other Directors. The value of each employee's total pay and benefits was calculated using the single figure methodology consistent with the Chief Executive, with the exception of the annual bonus, which was calculated using 2019 financial year bonuses (which were paid during 2020) where the 2020 financial year data was not available at the last practical date before the finalisation of this report. No elements of pay have been omitted. Where required, remuneration was approximately adjusted to reflect full-time and full-year equivalents based on the employees' contracted hours and the proportion of the year they were employed and not on furlough.

The following table provides salary and total remuneration information in respect of the employees at each quartile.

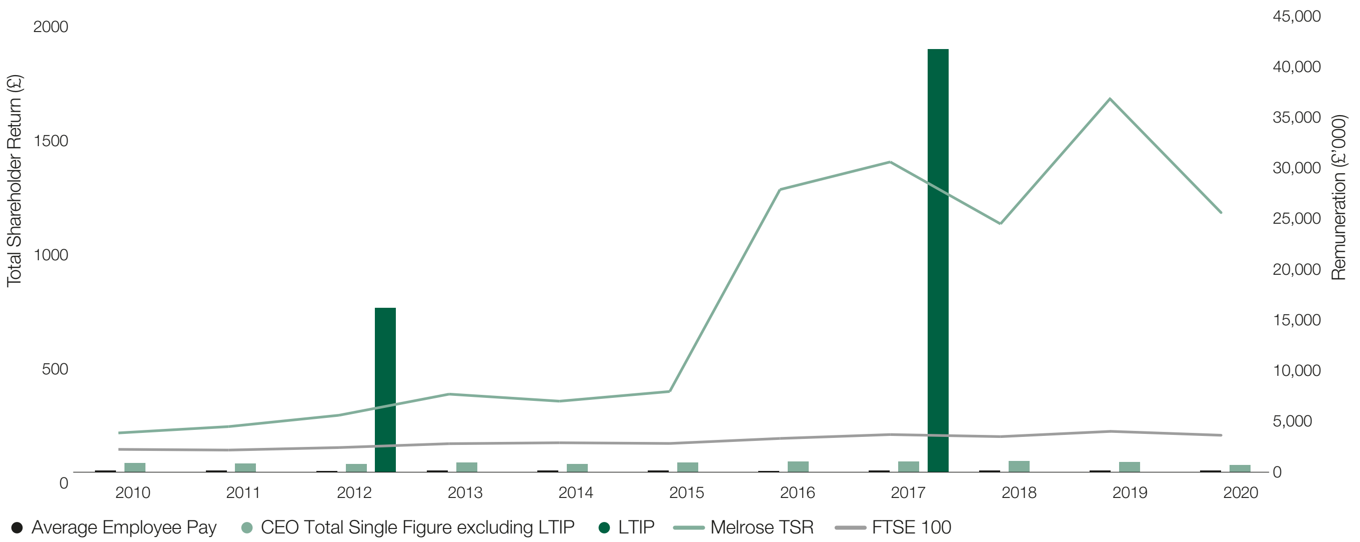
Financial year	Element of pay	25th percentile pay employee	Median employee	75th percentile employee
Year ended 31 December 2020	Salary and wages(1)	£30,000	£39,000	£50,000
	Total pay and benefits	£34,000	£42,000	£53,000

(1) Base salary includes overtime and shift allowances/premiums. The individual at the median received shift premium during the year.

All ratios have fallen since last year primarily as a result of the Chief Executive's salary being reduced for a significant part of the year due to COVID-19, and a reduction in the bonus awarded to the Chief Executive in relation to 2020 performance. In addition, the Chief Executive's long-term incentive arrangements, which represent the potential for significant opportunity in the executive remuneration structure, crystallised during the year for no value. Although COVID-19 also impacted pay for reward outcomes for employees, the scale of reduction for the Chief Executive was greater and this has therefore driven the reduction in the ratios. This year's continued low pay ratios reflect the relationship between the Chief Executive's pay and the experience of UK employees as a whole.

We have considered the pay data for the three employees identified and believe that it fairly reflects pay at the relevant quartiles amongst the UK workforce. The Committee considers that the median pay ratio is consistent with the relative role and responsibilities of the Chief Executive and the identified employee. Base salaries of all employees, including our executive Directors, are set with reference to a range of factors, including market practice, experience and performance in role. The Chief Executive's remuneration package is weighted towards variable pay due to the nature of the role, and this means that the ratio is likely to fluctuate depending on the outcomes of incentive plans in each year. The Chief Executive's remuneration package is otherwise very reasonable compared to the Company's FTSE 100 peers, which is also demonstrated on page 115 of this report. This is particularly relevant for the 2020 financial year where remuneration paid to the Chief Executive was significantly lower due to the impact of COVID-19 on the performance-related incentive elements of his pay, particularly the long-term incentive arrangements which crystallised for no value, and the temporary period of reduced salary. The ratio is therefore likely to be higher in following years.

To give context to the Chief Executive remuneration for the previous ten years and the CEO pay ratio, we have included an illustrative chart tracking CEO pay and average employee pay over the last ten financial years alongside Melrose's TSR performance and the FTSE 100's TSR performance over the same period. The Committee has always been committed to ensuring that the Chief Executive's reward is commensurate with performance. The chart shows a clear alignment between shareholder returns and the Chief Executive's single figure pay.



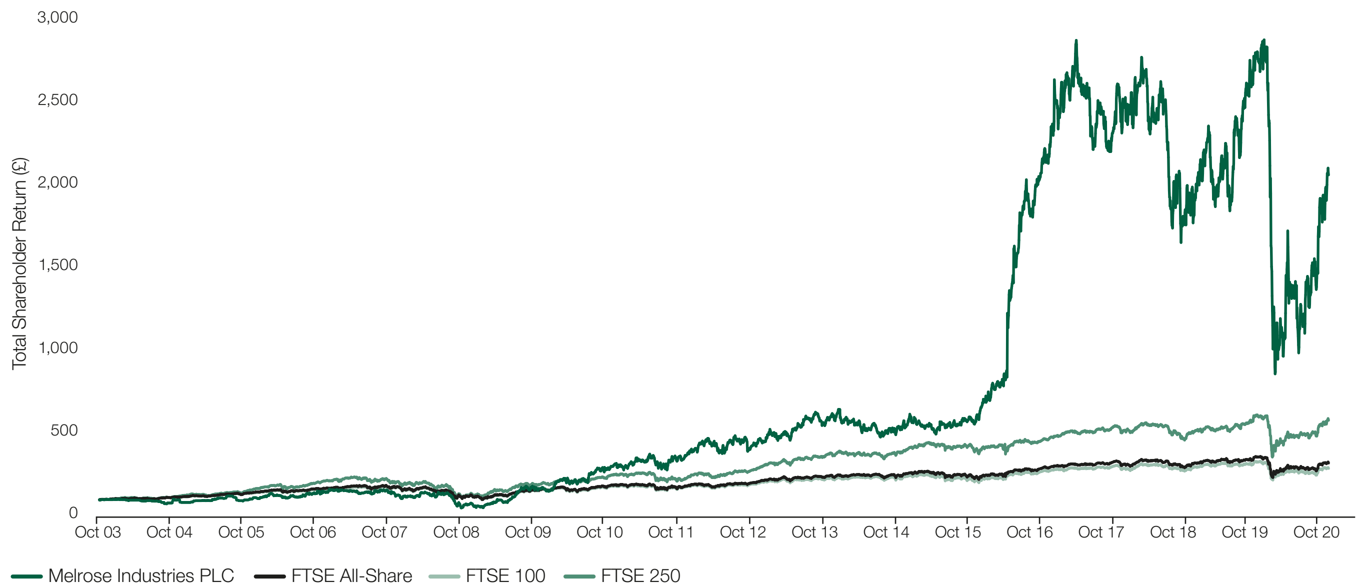
Percentage change in Directors' remuneration
The table below sets out, in relation to base salary, taxable benefits and annual bonus, the percentage increase in pay for each Director compared to the average increase for a group consisting of the Company's senior head office employees and the divisional CEOs, managing directors and finance directors of the Group's business units. The reporting legislation in this regard requires companies to publish the annual percentage change in the total remuneration of Directors and employees of the Company. The Company itself does not have any employees other than the executive Directors. However, in the interest of providing a relevant comparison to stakeholders, we choose to voluntarily disclose a comparison against the aforementioned group of senior management, which we consider to be an appropriate comparator group because of their level of seniority and the structure of their remuneration packages. The spread of the Company's operations across various countries and industries means that remuneration policies vary to take account of geography and industry such that the Committee considers that selecting a wider group of employees would not provide a meaningful comparison. The percentages shown relate to the financial year ended 31 December 2020 as a percentage comparison to the financial year ended 31 December 2019.

Element of remuneration	Basic salary/fee percentage change(1)	Additional fee percentage change(2)	Benefits percentage change(3)	Annual bonus percentage change(4)
Executive Directors				
Christopher Miller	-6%	n/a	-20%	n/a
David Roper	-6%	n/a	-8%	n/a
Simon Peckham	-6%	n/a	-2%	-71%
Geoffrey Martin	-6%	n/a	7%(5)	-72%
Non-executive Directors				
Justin Dowley	-6%	n/a	n/a	n/a
Liz Hewitt	-6%	29%(6)	n/a	n/a
David Lis	-6%	0%	n/a	n/a
Archie G. Kane	-6%	0%	n/a	n/a
Charlotte Twyning	-6%	n/a	n/a	n/a
Funmi Adegoke	278%(7)	n/a	n/a	n/a
Senior employees(8)	**-1%**	**n/a**	**11%**	**45%(9)**

(1) The annual percentage change is calculated by reference to actual basic salary or fee (as applicable) paid for the financial year ended 31 December 2020 compared to the financial year ended 31 December 2019. All Directors agreed to a temporary 20% reduction in their basic salary or fee (as applicable) during 2020 to support the Group's cash management strategy in light of COVID-19.
(2) This includes the additional fees for holding the position of Senior Independent Director, the Chairmanship of the Remuneration Committee, the Chairmanship of the Audit Committee, and the Chairmanship of the Nomination Committee.
(3) Benefits data is calculated on the same basis as the benefits data in the single total figure table. It does not include any pension allowances.
(4) The annual percentage change in bonus is calculated by reference to the bonus payable in respect of the financial year ended 31 December 2020 compared to the financial year ended 31 December 2019 for the applicable executive Directors, and by reference to all bonus payments received during the financial year ended 31 December 2020 in comparison to the financial year ended 31 December 2019 for senior employees. Neither the Executive Vice-Chairmen nor the Non-executive Directors are eligible to receive an annual bonus.
(5) This reflects an increase to the annual train travel fare.
(6) This reflects an increase to the additional fee for the Chairmanship of the Audit Committee, which was increased for 2020 to better reflect the increased scope and complexity of the role.
(7) Funmi Adegoke was appointed to the Board with effect from 1 October 2019. The increase in her basic fee from 2019 to 2020 reflects the pro-rated period of directorship in 2019 received for the period 1 October 2019 to 31 December 2019 versus a full year for 2020, so is not a meaningful comparison. If an annualised figure is assumed for her basic fee in 2019, the percentage change is -6%, the same as for the other Non-executive Directors.
(8) In light of the Company's business model of "Buy, Improve, Sell", this group of senior management inevitably varies from year to year, and can vary significantly in acquisition and disposal years.
(9) The change shown was impacted by legacy retention awards granted to GKN employees prior to our acquisition, a number of which crystallised during the period.

Total Shareholder Return
The total shareholder return graph below shows the value as at 31 December 2020 of £100 invested in the Company in October 2003, compared with £100 invested in the FTSE 100 Index, the FTSE 250 Index and the FTSE All-Share Index. This shows a TSR of 1,936% and demonstrates very clearly the long-term performance of the Company.

The Committee considers the FTSE 100 Index, the FTSE 250 Index and the FTSE All-Share Index to be appropriate indices for the year ended 31 December 2020 for the purposes of this comparison because of the comparable size of the companies which comprise the FTSE 100 Index and the FTSE 250 Index and the broad nature of companies which comprise the FTSE All-Share Index. The data shown below assumes that all cash returns to shareholders made by the Company during this period are reinvested in ordinary shares.



Directors' Remuneration report
Continued

Wider workforce considerations

Melrose is committed to creating an inclusive working environment and to rewarding our employees throughout the organisation in a fair manner. The Committee is mindful of wider workforce remuneration and conditions, and uses its awareness of these arrangements to ensure that Melrose executive pay is aligned with the Company's culture and strategy.

The Committee is responsible for setting the remuneration of the executive Directors and the Non-executive Chairman. It does not have responsibility for setting and managing the remuneration of Melrose senior management or divisional executive teams, which remain the responsibility of the Chief Executive, or the pay policies of the business units, responsibility for which sits with businesses themselves. The Committee remains of the view that such an approach is appropriate in light of Melrose's decentralised business model. The Committee does, however, have oversight of workforce pay, policies and incentives at a Melrose level and at a business unit executive level, which enables it to ensure that the approach taken to executive remuneration is consistent with those workforces. This consistency is evidenced by the 15% pension contribution and other benefits payable to the executive Directors, which are equal to those for Melrose employees and within the range of the benefits of the wider workforce. In addition, the CEO pay ratio continues to remain low, and we anticipate it remaining one of the lowest in the FTSE 100.

Given the differing nature of our businesses, the Committee does not expect a standardised approach to remuneration, nor would this be appropriate. However, when conducting its review, it does pay particular attention to whether each element of remuneration is consistent with the Company's remuneration philosophy. The Committee also receives confirmation from each business unit on an annual basis that the remuneration provided to its executive team is consistent with the remuneration provided to its wider workforce, and that the incentives operated by that business unit align with its culture and strategy. Based on these disclosures, the Committee is satisfied that the approaches taken to remuneration at all levels are consistent with the Company's remuneration philosophy.

Long-term incentives

Participation in the 2020 Employee Share Plan is limited to Melrose head office employees. However, we also recognise the need to appropriately incentivise the executive teams of our businesses, in order to ensure that they are invested in helping us to build stronger, better businesses. Consistent with Melrose's decentralised business model, divisional long-term incentive plans have been implemented for senior managers of certain of our business units, to incentivise them to create value for the Company and our shareholders. Depending on the amount of value created in relation to that particular business, participants in such incentive plans will receive a cash payment on the sale of the business. If a sale of the relevant business has not occurred within a certain period, the incentive plan will crystallise and any payment to be made to participants will be based on the increase in value of the business during this period.

Retirement provisions

The Company provides retirement benefits to Melrose employees and the business units determine the retirement benefits provided to their respective employees. The Group's commitments with regards to pension contributions are 15% of an employee's salary for members of the Melrose pension scheme, including the executive Directors, and these contributions are within the range of pension provisions across our various business unit UK pension schemes.

In line with the "Improve" aspect of Melrose's "Buy, Improve, Sell" strategy, we have continued to improve funding levels in the pension plans of our business units. As further detailed on page 5, Melrose has a stellar record of successfully taking underfunded pension schemes under our stewardship and bringing them to full funding. In particular, under Melrose ownership, the deficit under the GKN UK defined benefit pension schemes has reduced by over 80% to £0.1 billion.

Relative Importance of Spend on Pay

The following table sets out the percentage change in dividends and the overall expenditure on pay (as a whole across the Group).

Expenditure	Year ended 31 December 2019 £ million	Year ended 31 December 2020 £ million	Percentage change
Remuneration paid to all employees[1]	2,868	2,434	-15%
Distributions to shareholders by way of dividend and share buy back	231	0	-100%

(1) The figure for the year ended 31 December 2019 is the total staff costs as stated in note 7 to the financial statements and the figure for the year ended 31 December 2020 is the total staff costs as stated in note 7 to the financial statements. In light of the Company's business model of "Buy, Improve, Sell", your Board does not consider that the table is meaningful in the context of the Group's remuneration structure, which provides a strong alignment with shareholder interests.

Non-executive Directors

Single figure table and share interests (audited)

The following table sets out the single figure of remuneration for 2020 in comparison with 2019 for the Company's Non-executive Directors:

Non-executive Directors	Period	Total basic fees £000[1]	Total other fees £000[2]	Other (bonus, pension, LTIP, taxable benefits) £000	Total Fixed £000	Total Variable £000	Total £000
Justin Dowley (Chairman)	2020	330	0	n/a	**330**	**0**	**330**
	2019	350	0	n/a	**350**	**0**	**350**
Liz Hewitt (Senior Independent Director)	2020	71	45	n/a	**116**	**0**	**116**
	2019	75	35	n/a	**110**	**0**	**110**
David Lis	2020	71	20	n/a	**91**	**0**	**91**
	2019	75	20	n/a	**95**	**0**	**95**
Archie G. Kane	2020	71	10	n/a	**81**	**0**	**81**
	2019	75	10	n/a	**85**	**0**	**85**
Charlotte Twyning	2020	71	0	n/a	**71**	**0**	**71**
	2019	75	0	n/a	**75**	**0**	**75**
Funmi Adegoke[3]	2020	71	0	n/a	**71**	**0**	**71**
	2019	19	0	n/a	**19**	**0**	**19**
Total	**2020**	**685**	**75**	**n/a**	**760**	**0**	**760**
	2019	**669**	**65**	**n/a**	**734**	**0**	**734**

(1) Along with the executive Directors, all Non-executive Directors of the Company took a temporary 20% reduction in their basic fee payable during 2020 to support the Group's cash management strategy in light of COVID-19. The amounts stated in the table for 2020 are the actual amounts that were paid to the executive Directors.
(2) These are additional fees for holding the Chairmanship of the Remuneration Committee, the Audit Committee and the Nomination Committee, and for holding the position of Senior Independent Director. There are no additional fees payable for membership of a Committee. All of our Non-executive Directors are members of at least one Committee.
(3) Funmi Adegoke was appointed as a Non-executive Director of the Company with effect from 1 October 2019 and the fees referred to above for 2019 reflect her fees for the period 1 October 2019 to 31 December 2019.

The following table sets out the subsisting interests in the equity of the Company held by the Non-executive Directors as at 31 December 2020, as well as an indication as to the size of these interests relative to the entire issued share capital of the Company:

Non-executive Directors	Ordinary shares held as at 31 December 2020[1]	Shareholding (% ordinary share capital) as at 31 December 2020
Justin Dowley	1,568,395	0.0321%
Liz Hewitt	211,377	0.0044%
David Lis	458,947	0.0094%
Archie G. Kane	50,000	0.0010%
Charlotte Twyning	70,418	0.0014%
Funmi Adegoke	0	0%

(1) For these purposes, the interests of each Non-executive Director listed in the table include any ordinary shares held by a person closely associated with that Non-executive Director within the meaning of the EU Market Abuse Regulation, as it forms part of retained EU law by virtue of the European Union (Withdrawal) Act 2018.

Non-executive Directors' fees

Non-executive Directors' basic fees and the Non-executive Chairman's fee have been increased by 3% with effect from 1 January 2021, in keeping with increases made to executive Directors and other Melrose employees in previous years, and in line with other FTSE 100 companies. We note that while all Non-executive Directors serve on at least one of the Company's committees, there are no additional committee membership fees. As noted in the single figure table above, the Company remains of the view that it is not appropriate for our Non-executive Directors to receive any taxable benefits, pension contributions or variable remuneration.

The Non-executive Director fee levels for 2020 and 2021 are set out in the table below. We note that the basic Non-executive Director fee was subject to a temporary 20% reduction during 2020 due to COVID-19, in addition to the executive Director salaries, which explains the difference between the fees stated in the table below and the total fees shown in the single figure table above for 2020.

Fee element	Previous fee with effect from 1 January 2020	Fee with effect from 1 January 2021
Non-executive Chairman fee	£360,500	£371,315
Basic Non-executive Director fee	£77,250	£79,600
Additional fee for holding the Chairmanship of the Remuneration Committee	£20,000	£20,000
Additional fee for holding the Chairmanship of the Audit Committee	£30,000	£30,000
Additional fee for holding the Chairmanship of the Nomination Committee	£10,000	£10,000
Additional fee for holding the position of Senior Independent Director	£15,000	£15,000

Directors' Remuneration report
Continued

Service contracts and letters of appointment
Consistent with the best practice guidance provided by the Code, the Company's policy is for executive Directors to be employed on the terms of service agreements, which may be terminated by either the executive Director or the Company on the giving of not less than 12 months' written notice (subject to certain exceptions).

The executive Directors' service contracts do not provide for pre-determined compensation in the event of termination. Any payments made would be subject to normal contractual principles, including mitigation as appropriate. The length of service for any one executive Director is not defined and is subject to the requirement for annual re-election under both the Code and the Company's Articles of Association.

There is no unexpired term as each of the executive Directors' contracts is on a rolling basis.

The Non-executive Directors do not have service contracts but have letters of appointment for an initial term of three years, which may be renewed by mutual agreement. Generally, a Non-executive Director may be appointed for one or two periods of three years after the initial three-year period has expired, subject to re-election by shareholders at each AGM. The terms of appointment do not contain any contractual provisions regarding a notice period or the right to receive compensation in the event of early termination.

Each executive Director's service contract and each Non-executive Director's letter of appointment are available for inspection at the Company's registered office during normal business hours.

Details of the Non-executive Directors' terms of appointment are set out below:

Non-executive Directors	First appointment	Expires*
Justin Dowley (Chairman)	1 September 2011	AGM 2023
Liz Hewitt (Senior Independent Director)	8 October 2013	AGM 2022
David Lis	12 May 2016	AGM 2022
Archie G. Kane	5 July 2017	AGM 2021
Charlotte Twyning	1 October 2018	AGM 2021
Funmi Adegoke	1 October 2019	AGM 2022

* Subject to annual re-election.

Governance
Responsibilities
The Board has delegated to the Committee responsibility for overseeing the remuneration of the Chairman of the Board and the executive Directors.

The Committee's responsibilities include:
- Establishing and maintaining an executive Director remuneration policy that is appropriate, consistent and reflective of Melrose's remuneration philosophy.
- Determining the remuneration policy for the executive Directors.
- Setting and managing remuneration packages of the executive Directors and the Chairman of the Board in accordance with the Directors' Remuneration Policy.
- Overseeing the remuneration of Melrose senior management and divisional CEOs, to enable the Committee to consider their consistency with the executive Director remuneration packages.
- Operating the Company's long-term incentive arrangements.

As described on page 122, although they retain oversight, the Committee is not responsible for setting and managing the remuneration of Melrose senior management and divisional executive teams, nor is it responsible for determining wider business unit employee pay, which are the responsibility of the Chief Executive and the relevant business unit, respectively. Responsibility for determining the remuneration of the Non-executive Directors (other than the Chairman) sits with the Board. No Director plays a part in any decision about his or her own remuneration.

The Committee's terms of reference, which were last revised in November 2020, are available on our website, **www.melroseplc.net**, and from the Company Secretary at Melrose's registered office.

External evaluation
During 2020 an evaluation of the Chairman, the Board and its committees was undertaken in line with their respective terms of reference. These evaluations were conducted externally by Lintstock Ltd, a company unconnected with the Company and its Directors. The evaluation process involved direct engagement by Lintstock Ltd with each of the Directors. Lintstock Ltd prepared a report for the Board giving details of its evaluation and recommendations, and such report was subsequently discussed amongst the Board. The evaluation process demonstrated that the Board and its committees were operating effectively and the composition of such Boards and committees promoted the long-term sustainable success of the Company.

Attendance at meetings
The attendance of the Non-executive Directors at the scheduled meetings of the Committee in 2020 was as follows:

Member	No. of meetings(1)
David Lis (Chairman)	●● 2/2
Justin Dowley	●● 2/2
Archie G. Kane	●● 2/2
Charlotte Twyning	●● 2/2
Funmi Adegoke	●● 2/2

(1) Reflects regularly scheduled meetings of the Committee. An additional Committee meeting was held in October 2020 to discuss the 2020 Employee Share Plan proposal that was put to shareholders for approval at the end of 2020 (and approved at the general meeting held in January 2021). The meeting was attended by David Lis, Archie G. Kane and Charlotte Twyning, and the Chairman of the Committee separately discussed the proposals with the members of the Committee who were unable to join.

Compliance with legislation and the Code
We apply the principles of and are fully compliant with the key provisions of the Code and the Financial Conduct Authority's Listing Rules and Disclosure Guidance and Transparency Rules, including in relation to minimum shareholding requirements, post-cessation minimum shareholding requirements, pension alignment, malus and clawback, and discretion to override formulaic outcomes.

The Directors confirm that this report has also been prepared in accordance with the Companies Act 2006 and Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013.

As mentioned on page 112, the four principles of the Melrose remuneration structure are wholly aligned with the Code factors of clarity, simplicity, risk, predictability, proportionality and alignment to culture, as set out in the table below. The Committee ensured that it took all of these elements into account when establishing the Directors' Remuneration Policy, as well as its application to executive Directors during the period.

Factor	How the Remuneration Committee has addressed and link to strategy
Clarity	The Company's performance remuneration is based on supporting the implementation of the Company's strategy, which is primarily to create sustainable long-term shareholder value. This provides clarity to all stakeholders on the relationship between the successful implementation of the Company's strategy and the remuneration paid. The Company seeks to present its remuneration arrangements to investors in the clearest and most transparent way possible. We also remain committed to maintaining an open and transparent dialogue with our investors, both through formal engagement processes, ad hoc discussions, and through the disclosures in our annual reports.
Simplicity	The fixed elements of remuneration are limited to base salary, pension contribution and benefits, all below the lower quartile of peers and in the case of pension contributions, the same as other Melrose employees. There are only two variable elements of remuneration: the annual bonus and the 2020 Employee Share Plan, both of which are based on simple and transparent metrics. The operation of the Annual Bonus Plan is linked to an earnings-based target (at least 50%) and the achievement of strategic factors. The Company operates a single long-term incentive scheme, which simply rewards the creation of shareholder value over a three-year period above a minimum level of return for shareholders. In the Committee's view, this provides a very simple incentive framework which can be understood by all of the Company's stakeholders.
Risk	The Directors' Remuneration Policy includes the following elements to mitigate against the risk of target-based incentives: • Setting defined limits on the maximum award that can be earned, including capping the annual bonus to a maximum of 100% of base salary and the application of the annual rolling cap to the 2020 Employee Share Plan. • Requiring the deferral of up to 50% of the annual bonus award into ordinary shares of the Company in certain circumstances and that all of the ordinary shares awarded in relation to the 2020 Employee Share Plan (other than any ordinary shares sold in order to make adequate provision for any tax liability arising in connection with the crystallisation) be held for a two-year holding period following the crystallisation date. • The post-cessation minimum shareholding requirements, which require executive Directors to maintain the minimum shareholding for a period of two years after leaving the Company. • Aligning the performance condition with the "Buy, Improve, Sell" strategy of the Company. • Ensuring there is sufficient flexibility for the Committee to adjust payments through malus and clawback and an overriding discretion to depart from formulaic outcomes.
Predictability	Fixed remuneration for the executive Directors is set below the lower quartile of FTSE peers to limit fixed costs for the Group, to provide certainty and to incentivise executive Directors. Variable remuneration is limited to the annual bonus, which is capped at 100% of salary and performance-driven based on financial growth and strategic factors, and the 2020 Employee Share Plan. The Committee set out the possible values that may be earned under the 2020 Employee Share Plan upon approval of the plan by shareholders, and will update this every year. The method of calculation, limits and discretions under the Directors' Remuneration Policy are clearly set out.
Proportionality	The restricted fixed remuneration and capped Annual Bonus Plan is compensated by the opportunity for potentially significant reward entirely dependent on performance pursuant to the 2020 Employee Share Plan that supports the Company's value creation strategy.
Alignment to culture	The focus on responsible stewardship and long-term sustainable performance is a key part of the Company's culture. This is supported by the Directors' Remuneration Policy, which (i) facilitates Committee oversight of workforce pay, policies and incentives; (ii) aligns executive Director contributions to those provided to the rest of the Melrose employees; and (iii) deliberately restricts the annual salaries, bonuses and benefits for the executive Directors well below the lower quartile of the FTSE 100.

Directors' Remuneration report

Continued

Committee membership
All members of the Committee are independent Non-executive Directors within the definition of the Code. None of the Committee members have any personal financial interest (other than as shareholders in the Company) in matters to be decided, nor do they have any conflicts of interest from cross-directorships or any day-to-day involvement in running the business.

Advisors to the Remuneration Committee
During the year, the Committee received advice on the remuneration reporting regulations and support in the review of the Directors' Remuneration Policy from PwC LLP. PwC LLP's fees for this advice were £37,250 excluding VAT, which were charged on a time/cost basis. During the year, PwC LLP also provided the Company with reward, tax, accounting, and consulting advice.

PwC LLP have been appointed by the Committee to act as its remuneration consultants and were reappointed to act for the period under review. PwC LLP is a member of the Remuneration Consultants Group, and as such chooses to operate pursuant to a code of conduct that requires remuneration advice to be given objectively and independently. The Committee is satisfied that the advice provided by PwC LLP in relation to remuneration matters is objective and independent.

The Company Secretary acts as secretary to the Committee and attends Committee meetings.

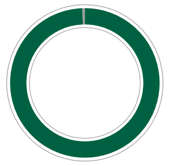
Statement of voting at general meetings
The charts below set out the votes on the Annual Report on Remuneration at the 2020 AGM, on the Directors' Remuneration Policy at the 2020 AGM, and on the 2020 Employee Share Plan and the consequential amendments to the Directors' Remuneration Policy at the January 2021 general meeting.

This Annual Report on Remuneration will be put to an advisory vote at the AGM, on 6 May 2021.

Resolution to approve the Directors' Remuneration Report for the year ended 31 December 2019 (7 May 2020)

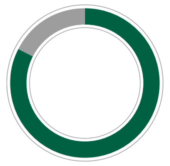
Percentage of votes cast for the resolution	99.57%
Percentage of votes cast against the resolution	0.43%
Votes withheld 77,371,889	

Resolution to approve the Directors' Remuneration Policy (7 May 2020)



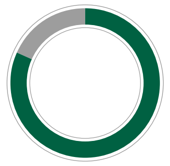
Percentage of votes cast for the resolution	98.40%
Percentage of votes cast against the resolution	1.60%
Votes withheld 422,042,417	

Resolution to approve and implement the 2020 Employee Share Plan (21 January 2021)



Percentage of votes cast for the resolution	82.64%
Percentage of votes cast against the resolution	17.36%
Votes withheld 228,313,488	

Resolution to approve the amendments proposed to the 2020 Directors' Remuneration Policy to accommodate the 2020 Employee Share Plan (21 January 2021)



Percentage of votes cast for the resolution	81.81%
Percentage of votes cast against the resolution	18.19%
Votes withheld 108,963,824	

This report was approved by the Board and signed on its behalf by:

David Lis
Chairman, Remuneration Committee
4 March 2021

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law, the Directors are required to prepare the Group financial statements in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and with International Financial Reporting Standards (IFRSs) adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union. The financial statements also comply with IFRSs as issued by the IASB. The Directors have also chosen to prepare the parent company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland". Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing the parent company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

In preparing the Group financial statements, International Accounting Standard 1 requires that Directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a strategic report, directors' report, directors' remuneration report and corporate governance statement, each of which complies with law and regulation.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' responsibility statement

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the Strategic Report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the Annual Report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

This responsibility statement was approved by the Board of Directors on 4 March 2021 and is signed on its behalf by:

Geoffrey Martin
Group Finance Director
4 March 2021

Simon Peckham
Chief Executive
4 March 2021

Independent auditor's report to the members of Melrose Industries PLC

Report on the audit of the financial statements

1. Opinion

In our opinion:

- the financial statements of Melrose Industries PLC (the 'parent company') and its subsidiaries (the 'group') give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2020 and of the group's loss for the year then ended;
- the group financial statements have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006 and International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland"; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the Consolidated Income Statement;
- the Consolidated Statement of Comprehensive Income;
- the Consolidated Statement of Cash Flows;
- the Consolidated and Parent Company Balance Sheets;
- the Consolidated and Parent Company Statements of Changes in Equity; and
- the related notes 1 to 30 and the related notes 1 to 8 to the Parent Company Balance Sheet.

The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and international accounting standards in conformity with the requirements of the Companies Act 2006 and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 102 "The Financial Reporting Standard applicable in the UK and Republic of Ireland" (United Kingdom Generally Accepted Accounting Practice).

2. Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. The non-audit services provided to the group and parent company for the year are disclosed in note 7 to the financial statements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

3. Summary of our audit approach

Key audit matters	The key audit matters that we identified in the current year were: • Impairment of goodwill and acquired intangibles; • Classification of adjusting items; • Revenue recognition in respect of RRSPs; and • Valuation of loss-making contract provisions.	Within this report, key audit matters are identified as follows: Newly identified Increased level of risk Similar level of risk Decreased level of risk
Materiality	The materiality that we used for the group financial statements was £30 million which was determined on the based on a number of benchmarks including adjusted profit before tax, net assets and revenue.	
Scoping	We selected 29 reporting units where we requested component auditors to perform a full scope audit of the components' financial information. We also requested component auditors to audit certain account balances and transactions ("SAB") at a further 23 reporting units. Finally we requested that component auditors perform specified audit procedures ("SAP") on a further 7 reporting units. Coverage from full scope, SAB and SAP scope components totals 80% of the group's revenue, 83% of adjusted operating profit and 93% of net assets.	
Significant changes in our approach	Inventory valuation in Aerospace is no longer considered a key audit matter due to the reduction in value of the inventories held at the sites where a significant audit risk in inventory valuation was pinpointed to in the prior year. Our approach to scoping has changed slightly since the prior year, with a new category of scoped reporting unit identified. We now have full scope, audit of certain account balances and transactions (SAB) and specified audit procedures (SAP). SAP components differ from SAB components according to the size and risks associated with the particular entities. Our approach to materiality has changed for FY20 due to the impact of the Covid-19 pandemic on the group's financial performance. This has been discussed in more detail in section 6.	

4. Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Our evaluation of the directors' assessment of the group's and parent company's ability to continue to adopt the going concern basis of accounting included assessment of the following:

- obtained understanding of the financing facilities including nature of facilities, repayment terms and covenants;
- assessed the impact of risk and uncertainties on the business model and future cash flow forecasts;
- considered as part of our assessment the nature of the group, its business model and related risks including where relevant the impact of Covid-19 and Brexit, the requirements of the applicable financial reporting framework and the system of internal control;
- evaluated the directors' assessment of the group's ability to continue as a going concern, including challenging the underlying data and key assumptions used to make the assessment, and evaluated the directors' plans for future actions in relation to their going concern assessment. This was done through detailed assessment of the operating and non-operating cash flows for reasonableness and consistency with the underlying forecast and plans for individual businesses;
- assessed the sufficiency headroom available in the forecasts (cash and covenants) with respect to the risks and uncertainties;
- assessed management's sensitivity analysis in order to assess whether that the reasonable worst case sensitivities capture all the reasonably possible downside risks and uncertainties; and
- assessed the adequacy of the disclosures provided in the financial statements.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the group's and parent company's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

In relation to the reporting on how the group has applied the UK Corporate Governance Code, we have nothing material to add or draw attention to in relation to the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Independent auditor's report to the members of Melrose Industries PLC
Continued

5. Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

5.1 Impairment of Goodwill and acquired intangibles

Key audit matter description

Goodwill on the balance sheet at 31 December 2020 is £3,640 million (2019: £3,653 million), and the acquired intangible assets balance is £5,150 million (2019: 5,689 million). The risk associated with the impairment of Goodwill and acquired intangibles has increased in the year to the adverse impact of Covid-19 on the group's performance during the year and its pervasive impact on the future outlook of Aerospace and Automotive industries. As required by IAS 36 Impairment of assets ("IAS 36") management performs an impairment review for all goodwill balances on an annual basis and for other assets whenever an indication of impairment is identified. This review identified the following groups of CGUs where headroom is limited and sensitive to changes in key assumptions:

- Aerostructures (goodwill £605 million, other intangible assets £1,020 million)
- Aerospace Engine Systems (goodwill £337 million, other intangible assets £1,773 million)
- Automotive ePowertrain (goodwill £336 million, other intangible assets £488 million)
- Automotive Driveline (goodwill £690 million, other intangible assets £658 million)
- Powder Metallurgy (goodwill £524 million, other intangible assets £628 million)
- Nortek Control (goodwill £167 million, other intangible assets £109 million)
- Ergotron (goodwill £406 million, other intangible assets £67 million)

Headroom available at 31 December 2020 has decreased considerably for the CGUs noted above. This has been identified as a key audit matter as a result of the quantitative significance of the balances, and the application of management judgement and estimation in performing impairment reviews for these groups of CGUs in particular, specifically with respect to:

- The selection of the appropriate methodology (fair value less costs to sell or value in use) in determining recoverable amount for each group of CGUs;
- the effect on future cash flows of the pace of recovery of the Aerospace industry;
- the margin improvements as a result of restructuring programmes (implemented in 2020 and forecast to be implemented in the future across Aerostructures, Aerospace Engine Systems, Powder Metallurgy, Automotive Driveline and Automotive ePowertrain); and
- determination of the correct discount and growth rates to be used in the model.

Further details are included in note 11 to the financial statements in relation to the sensitivities reflecting the risks inherent in the valuation of goodwill and other non-current assets and also in note 3 to the financial statements in relation to the key sources of estimation uncertainty for these businesses.

Refer also to page 104 of the report of the audit committee.

How the scope of our audit responded to the key audit matter

We obtained an understanding of the relevant controls over the valuation of goodwill and other intangible assets, in particular the relevant controls over the forecasts that underpin the value in use and fair value less cost to sell models and controls around management's preparation of impairment models.

We assessed management's impairment paper, underlying analysis and supporting financial models, and challenged the reasonableness of the assumptions that underpin management's forecasts. Specifically, our work included, but was not limited to:

- assessed the methodology selected by management to estimate recoverable amount (fair value less cost to sell or value in use) against the requirements of IAS 36 and IFRS 13 Fair value measurement;
- understood management's process for assessing the impact on operating margin of ongoing and future restructuring programmes and challenged the benefit assumed by benchmarking against previous restructuring programmes;
- challenged management's assumptions within the impairment models, particularly forecast cash flows and how management will achieve improvements to operating margin through ongoing restructuring programmes;
- benchmarked long term growth rates to applicable macro-economic and market data, also taking into account the assumed recovery post Covid-19 outbreak in 2020;
- involved our internal valuation specialists to challenge the discount rate applied, by obtaining the underlying data used in the calculation and benchmarking it against market data and comparable organisations, and by evaluating the underlying process used to determine the risk adjusted cash flow projections;
- checked the integrity of the impairment models through testing of the mathematical accuracy, checking the application of the input assumptions and testing its compliance with IAS 36;
- performing sensitivity analysis to identify the key assumptions that have a significant effect on the model;
- assessed for appropriateness, all the reorganisations made in the CGUs for Aerospace and Automotive divisions. Furthermore, we assessed whether that the change in impairment assessment dates is in line with the requirements of IAS 36; and
- assessed the appropriateness of the sensitivity disclosures included by management in note 11 to the financial statements, challenging management's choice regarding the assumptions to be sensitised, and re-performing the underpinning calculations.

Key observations

The results of the impairment tests demonstrated that the recoverable amount is dependent on the success of restructuring plans and consequent improvement in margins for Aerostructures, Aerospace Engine Systems, Powder Metallurgy, Automotive Driveline, Automotive ePowertrain, Nortek Controls and Ergotron, and recovery of the Aerospace and automotive market more broadly.

We determined that the assumptions applied in the impairment model were within an acceptable range, that the overall position adopted was reasonable and that the disclosures in respect of sensitivity to reasonably possible changes to key assumptions are appropriate.

5.2 Classification of adjusting items

Key audit matter description

In addition to the statutory results, the group continues to present adjusted profit measures which are before the impact of adjusting items. Judgements made by management regarding the classification of adjusting costs and income therefore have a significant impact on the presentation of the group's results. In total, adjustments of £678 million have been made to the statutory operating loss of £338 million to derive adjusted operating profit of £340 million.

Adjusting items included:

- amortisation of acquisition-related intangible assets (£526 million);
- restructuring costs (£220 million);
- impairment of assets (£184 million);
- equity accounted investments adjustments (£30 million);
- equity settled compensation scheme charges (£11 million);
- acquisition and disposal costs (£5 million);
- impact of GMP equalisation (£2 million)
- gain on movement in fair value of derivatives (£182 million); and
- income from releases and changes in discount rate of fair value items (£118 million);

A key audit matter has been identified in respect of the classification of items recorded as adjusting. While the key measure used by management to monitor performance is adjusted operating profit, adjusted profit before tax is also a key measure used by management in communication with shareholders. There is a risk that items may be classified as adjusting which are underlying or recurring items, and therefore distort the reported adjusted profit, whether due to manipulation or error. Consistency in the identification and presentation of these items is important for the comparability of year on year reporting.

Explanations of each adjustment are set out in note 6 to the financial statements. Refer also to page 105 (Report of the audit committee).

How the scope of our audit responded to the key audit matter

We obtained understanding of the relevant controls over the classification of adjusting items in the financial statements.

We evaluated the appropriateness of the inclusion of items, both individually and in aggregate, within adjusted results. Specifically, we:

- assessed the consistency of items included year on year and the application of management's accounting policy, challenging the nature of these items in comparison to ESMA guidance and latest FRC guidance, and challenging in particular the inclusion of those items that recur annually;
- tested a sample of adjusting items by agreeing to source documentation and evaluating their nature in order to assess whether they are disclosed in accordance with the group's accounting policy, and also to assess consistency of adjusting items between periods in the financial statements;
- focussed our challenge on certain categories within adjusted items where we assessed that increased level of judgement had been applied by management, and there was increased opportunity for fraud or error. This included additional testing of restructuring costs, movements in fair value adjustments and impairment of assets;
- agreed the amounts recorded through to underlying financial records and other audit support to test that the amounts disclosed were complete and accurate;
- tested that the asset impairments included in adjusting items include specific fixed assets, inventory, and other assets write offs and are allowed to be so included under the group's existing policy;
- where management recognised releases to fair value adjustments, we challenged this classification and assessed whether events and conditions existed to cause a release of the provision recognised as part of acquisition accounting;
- for restructuring costs, assessed whether that the recognised costs meet the recognition criteria set out in IAS 37 'Provisions'; and
- assessed whether the disclosures within the financial statements provide sufficient detail for the reader to understand the nature of these items and how adjusted results are reconciled to statutory results.

Key observations

The value of adjusting items results in a material difference between the statutory and adjusted results. Whilst we note that the majority of adjusting items recur from period to period, their classification and presentation is consistent with the Group's policy.

Independent auditor's report to the members of Melrose Industries PLC
Continued

5.3 Revenue Recognition in respect of RRSPs

Key audit matter description	The group has recognised total revenue of £8,770 million in 2020 (2019: £10,967 million). There are judgements taken within the revenue recognition of material Risk and Revenue Sharing Partnerships ("RRSPs") in the Aerospace division (where revenue totals £2,804 million (2019: £3,852 million)). The risk specifically arises in the Engine Systems businesses and focuses on the timing at which performance obligations are met as well as the valuation of revenue recognised given the increased level of estimation and judgement on application of principles set out in IFRS 15 Revenue from contracts with customers. This includes the revenue recognised from those contracts identified by management where the pricing for the same parts varies across the contract. There is judgement in how the overall price is allocated across the units supplied where there is a contractual right to aftermarket revenues. The amount of revenue recognised from RRSP contracts during the year was £354 million, which includes variable consideration of £13 million (2019: £679 million, which included variable consideration of £45 million). Furthermore, the revenue recognition models used by management for RRSPs involve a number of significant assumptions based on any modifications to the contracts and historical data and trends, such as engineering requirements to support programmes and the expected life of mature engines. Any changes to these assumptions requires a higher level of judgement and estimation. This increases the risk that revenue recognition may not be appropriate. Refer to page 105 (Report of the audit committee) and page 153 (note 3 to the financial statements) and page 154 (note 4 to the financial statements).
How the scope of our audit responded to the key audit matter	We obtained an understanding of the relevant controls over the recognition of revenue for RRSP contracts. For each RRSP contract with material variable consideration, we recalculated the amount of revenue recognised to assess that it has been calculated in accordance with IFRS 15, the contractual agreement and the latest correspondence with the customer. In particular, we have: • agreed the percentage of revenue entitlement to the customer contract; • reviewed correspondence with the customer in the period, in particular entitlement reports; • challenged estimations made by management at the year end by taking account of historical settlements and checking historical estimation accuracy; • challenged the assumptions used in arriving at the element of variable consideration recognised. This was done by performed a number of procedures listed below; • performed an assessment of the timing at which control is transferred and revenue is recognised by identifying the performance obligations from the contract and checking the recognition triggers; • obtained and checked the contract modifications, including programme share or changes in pricing, and tested that they have been appropriately included in the RRSP models; and • tested underlying data included in the trend analysis above and performed independent industry research for evidence that may contradict management's assumptions on margin and engine life. In assessing the key assumptions in the revenue recognition model, we performed specific procedures that included: • obtained an understanding of the relevant controls in place within the Aerospace business to review the underlying data; • challenged and assessed the position papers prepared by management, and the model prepared; • assessed accuracy of the underlying data that has been used in the determination of the assumptions including usage profiles, industry data and customer correspondence; and • assessed the disclosure provided in the financial statements in relation to the changes in these assumptions against the requirements of IFRS 15.
Key observations	We are satisfied that the key assumptions made in determining the value of revenue recognised on RRSP contracts with variable consideration were within an acceptable range and the overall position was reasonable. We consider the disclosure provided in the financial statements in relation to the changes in the key assumptions is appropriate and consistent with the requirements of IFRS 15.

5.4 Valuation of Loss-making contracts provision

Key audit matter description	In 2018, upon acquisition of GKN, the group recognised provisions of £629 million in relation to loss-making contracts. At 31 December 2020, following utilisation and release during the year, £241 million remained unutilised (2019: £384 million). The methodology supporting the provisions is inherently complex and involves a high level of management judgement and estimation. We consider the following to be the key judgements and estimates in relation to these provisions: • accounting for the effect of negotiations and correspondence with customers on the existing loss-making contracts provision; • forecast cost projections including the level of material, direct labour and contract-related overheads; • calculation of utilisation for the year; • assessing changes in inputs and assumptions to evaluate whether the correct timing of releases; and • the classification of provision utilisation and release. Refer to page 105 (of the audit committee report) and page 153 (note 3 to the financial statements and page 175 (note 21 to the financial statements).
How the scope of our audit responded to the key audit matter	We obtained an understanding of the relevant controls over the review and estimation of loss-making contract provisions. For a sample of loss-making contract provision balances (including all material provisions) our work included, but was not limited to: • obtaining and checking supporting documentation for key assumptions and inputs, for example: – price data from corresponding contracts; – volumes from independent and recognised industry reports; – invoice and supplier documentation that supports costs; and – executed agreements for changes to pricing or early termination of contracts and other terms; • enquiry of legal, commercial, operational, programme and engineering management to understand any changes to the relevant programmes that would impact valuation (e.g. new tooling, manufacturing improvements and efficiencies, changes in raw material costs); • checking relevant third party correspondence (with customers and suppliers) and assessed the impact on the valuation of the provision; • recalculating the amount of the provision utilised in the year, and testing assumptions and inputs used to calculate utilisation; • for any releases of provisions, challenging the judgements applied by management and examined appropriate evidence supporting the release (new commercial agreements, price amendments, support for cost reductions such as labour cost and direct overheads savings etc); and • evaluating whether that the releases and utilisation are classified in accordance with the accounting policy.
Key observations	We are satisfied that the loss-making contracts provision at 31 December 2020 is valued appropriately, that releases and utilisation recorded during the year were appropriate, and that key estimates formed by management are reasonable.

6. Our application of materiality

6.1 Materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
Materiality	£30 million (2019: £42 million)	£15 million (2019: £8.7 million)
Basis for determining materiality	We considered the following metrics: • adjusted profit before tax; • revenue; and • net assets. Using professional judgment we determined materiality to be £30m. In the prior year, materiality was determined on the basis of 5% of adjusted profit before tax.	We determined materiality based on net assets, which was then capped at 50% (2019: 35%) of group materiality in order to address the risk of aggregation when combined with other businesses.
Rationale for the benchmark applied	In determining our benchmark for materiality we considered a number of different metrics used by investors and other readers of the Financial Statements. This approach is a change from the prior year to reflect the volatility in the results of the group arising from the impact of Covid-19. Materiality for the current year represents: • 19.6% of adjusted profit before tax (FY19: 4.7%); • 0.3% of revenue (FY19: 0.4%); and • 0.4% of net assets (FY19: 0.6%).	In our professional judgement we believe that use of a balance sheet measure is appropriate for a holding company. This is with reference to the net asset position of the company when compared to the net asset position of the group.

Independent auditor's report to the members of Melrose Industries PLC
Continued

6.2 Performance materiality
We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole.

	Group financial statements	Parent company financial statements
Performance materiality	60% (2019: 60%) of group materiality	60% (2019: 60%) of parent company materiality
Basis and rationale for determining performance materiality	• the assessment of the complexity of the group and nature of the group's business model; and • the de-centralised nature of the group's control environment and its variation across the group.	

6.3 Error reporting threshold
We agreed with the audit committee that we would report to the committee all audit differences in excess of £1.5 million (2019: £2 million), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the audit committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

7. An overview of the scope of our audit
7.1 Identification and scoping of components
In order to determine the scoping of components we consider the nature of the Group and its structure. There are now five operating segments in the continuing operations of the group:
- Aerospace;
- Automotive;
- Powder Metallurgy;
- Nortek Air Management; and
- Other Industrial (which consists of Brush, Nortek Control, and Ergotron)

In addition to the operating segments above, the group has a number of central cost centres which report to the Board and include head office companies for corporate functions and costs.

Each division consists of a number of reporting units, and manages operations on a geographical and functional basis. There are 326 reporting units in total, each of which is responsible for maintaining their own accounting records and controls and using an integrated consolidation system to report to UK head office. Our group audit scope focused on audit work at 60 components (2019: 68), of which
- 17 relate to components that form part of the Aerospace segment;
- 19 relate to components that form part of the Automotive segment;
- 5 relate to components that form part of the Powder Metallurgy segment;
- 7 relate to components that form part of the Nortek Air management;
- 5 relate to components that form part of the Other Industrial segment; and
- 7 relate to corporate cost centres.

Each component was set a specific component materiality, considering its relative size and any component-specific risk factors such as internal audit findings and history of error. The component materialities applied were in the range £7 million to £16 million.

We selected 29 reporting units where we requested component auditors to perform a full scope audit of the components' financial information. We also requested component auditors to audit certain account balances and transactions ("SAB") at a further 23 reporting units. Finally we requested component auditors to perform specified audit procedures ("SAP") on a further 7 reporting units. Coverage from full scope, SAB and SAP scope components totals 80% of the group's revenue, 79% of adjusted operating profit and 94% of net assets.

Aerospace
In respect of the Aerospace division, 5 components were subject to a full audit and 11 components were subject to SAP and SAB scope. These 16 components together accounted for 79% of the Aerospace division's revenue and 80% of the Aerospace division's adjusted operating profit and divisional costs.

Automotive
In respect of the Automotive division, 8 components were subject to a full audit and 11 components were subject to SAP and SAB scope. These 19 components accounted for 83% of the Automotive division's revenue and 99% of the Automotive division's adjusted operating profit and divisional costs.

Powder Metallurgy
In respect of the Powder Metallurgy division, 1 component was subject to a full audit and 4 components were subject to SAB scope. These 5 components together accounted for 73% of the Powder Metallurgy division's revenue and 78% of the Powder Metallurgy division's adjusted operating profit and divisional costs.

Nortek Air management
In respect of the Nortek Air management division, 7 components were subject to a full audit. These 7 components together accounted for 100% of the Nortek Air management division's revenue and 79% of the Nortek Air Management's adjusted operating profit and divisional costs.

Other Industrial
In respect of the Other Industrial division, 4 components were subject to a full audit. These 4 components together accounted for 50% of the Other Industrial division's revenue and 84% of the Other Industrial division's adjusted operating profit and divisional costs.

Corporate cost centres
In respect of the corporate cost centres, 4 components were subject to a full audit and 3 components were subject to SAB scope.

Company
The audit of the Company was performed by the group engagement team based at the Company's head office.

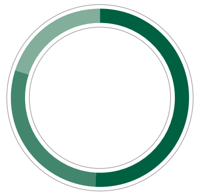
Residual balances
All entities not subject to the audit procedures above were subject to analytical procedures by the group engagement team.

While we understood and tested design and implementation of relevant controls in key areas, given the number and diverse nature of the components of the group, we took controls reliance in certain limited areas of the audit only.

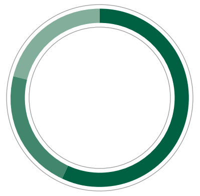
7.2 How we worked with other auditors
Due to restrictions on working practices caused by Covid-19 the majority of the audit work was executed remotely. No sites were visited due to the restrictions to travel. Instead, regular communication took place with component audit teams and component management teams using conference and video calls, with a particular focus on locations where work was performed on significant audit risks.

In addition to the above, the senior statutory auditor held group-wide, divisional and individual planning and close meetings which covered all businesses. Each division has a dedicated senior member of the group audit team responsible for the supervision and direction of components, including where appropriate sector-specific expertise. We included the component audit teams in our team briefing, discuss and review their risk assessment, and reviewed documentation of the findings from their work. We also reviewed the audit work papers supporting component teams' reporting to us remotely using shared desktop technology.

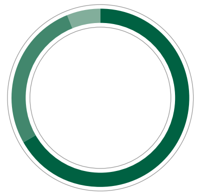
Revenue



Adjusted operating profit



Net assets



8. Other information
The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit, or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

9. Responsibilities of directors
As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

10. Auditor's responsibilities for the audit of the financial statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Independent auditor's report to the members of Melrose Industries PLC

Continued

11. Extent to which the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

11.1 Identifying and assessing potential risks related to irregularities

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, we considered the following:

- the nature of the industry and sector, control environment and business performance including the design of the group's remuneration policies, key drivers for directors' remuneration, bonus levels and performance targets;
- results of our enquiries of management, internal audit, legal counsel, operational staff and the audit committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the group's documentation of their policies and procedures relating to:
  - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
  - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
  - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations; and
- the matters discussed among the audit engagement team including significant component audit teams and involving relevant internal specialists, including tax, valuations, pensions and IT specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in the following areas: impairment of goodwill and acquired intangibles, classification of adjusted items, revenue recognition in respect of RRSPs and valuation of loss-making contracts provisions. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory frameworks that the group operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the financial statements. The key laws and regulations we considered in this context included the UK Companies Act and Listing Rules, UK Bribery Act as well as pensions legislation and tax legislation.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the group's ability to operate or to avoid a material penalty. These included the group's environmental regulations in the jurisdictions the group operates in.

11.2 Audit response to risks identified

As a result of performing the above, we identified the following key audit matters: impairment of goodwill and intangibles, classification of adjusted items, revenue recognition in respect of RRSPs and valuation of loss-making contracts provision as key audit matters related to the potential risk of fraud. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters. In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with provisions of relevant laws and regulations described as having a direct effect on the financial statements;
- enquiring of management, the audit committee and in-house legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with HMRC; and
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists and significant component audit teams, and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

Report on other legal and regulatory requirements

12. Opinions on other matters prescribed by the Companies Act 2006

In our opinion the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the group and the parent company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

13. Corporate Governance Statement

The Listing Rules require us to review the directors' statement in relation to going concern, longer-term viability and that part of the Corporate Governance Statement relating to the group's compliance with the provisions of the UK Corporate Governance Code specified for our review.

Based on the work undertaken as part of our audit, we have concluded that each of the following elements of the Corporate Governance Statement is materially consistent with the financial statements and our knowledge obtained during the audit:

- the directors' statement with regards to the appropriateness of adopting the going concern basis of accounting and any material uncertainties identified set out on page 42;
- the directors' explanation as to its assessment of the group's prospects, the period this assessment covers and why the period is appropriate set out on page 43;
- the directors' statement on fair, balanced and understandable set out on page 127;
- the board's confirmation that it has carried out a robust assessment of the emerging and principal risks set out on page 44;
- the section of the annual report that describes the review of effectiveness of risk management and internal control systems set out on page 45; and
- the section describing the work of the audit committee set out on page 103.

14. Matters on which we are required to report by exception

14.1 Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made or the part of the directors' remuneration report to be audited is not in agreement with the accounting records and returns.

We have nothing to report in respect of these matters.

15. Other matters which we are required to address

15.1 Auditor tenure

Following the recommendation of the audit committee, we were appointed by the Board of Directors in 2003 to audit the financial statements for the year ending 31 December 2003 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is 18 years, covering the years ending 31 December 2003 to 31 December 2020.

15.2 Consistency of the audit report with the additional report to the audit committee

Our audit opinion is consistent with the additional report to the audit committee we are required to provide in accordance with ISAs (UK).

16. Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Edward Hanson (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom

4 March 2021

Consolidated Income Statement

Continuing operations	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue	4, 5	**8,770**	10,967
Cost of sales		**(7,492)**	(8,732)
Gross profit		**1,278**	2,235
Share of results of equity accounted investments	15	**32**	38
Net operating expenses	7	**(1,648)**	(1,955)
Operating (loss)/profit	5, 6	**(338)**	318
Finance costs	7	**(200)**	(221)
Finance income	7	**3**	9
(Loss)/profit before tax		**(535)**	106
Tax	8	**12**	(51)
(Loss)/profit after tax for the year from continuing operations		**(523)**	55
Discontinued operations			
Loss for the year from discontinued operations	13	**(10)**	(106)
Loss after tax for the year		**(533)**	(51)
Attributable to:			
Owners of the parent		**(536)**	(60)
Non-controlling interests		**3**	9
		(533)	(51)
Earnings per share			
Continuing operations			
– Basic	10	**(10.8)p**	0.9p
– Diluted	10	**(10.8)p**	0.9p
Continuing and discontinued operations			
– Basic	10	**(11.0)p**	(1.2)p
– Diluted	10	**(11.0)p**	(1.2)p
Adjusted[1] results from continuing operations			
Adjusted revenue	5	**9,361**	11,592
Adjusted operating profit	5, 6	**340**	1,102
Adjusted profit before tax	6	**153**	889
Adjusted profit after tax	6	**120**	699
Adjusted basic earnings per share	10	**2.4p**	14.3p
Adjusted diluted earnings per share	10	**2.4p**	14.3p

(1) Defined in the summary of significant accounting policies (note 2).

Consolidated Statement of Comprehensive Income

	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Loss after tax for the year		**(533)**	(51)
Items that will not be reclassified subsequently to the Income Statement:			
Net remeasurement gain/(loss) on retirement benefit obligations	24	**244**	(32)
Fair value loss on investments in equity instruments	12	**(16)**	–
Income tax (charge)/credit relating to items that will not be reclassified	8	**(42)**	15
		186	(17)
Items that may be reclassified subsequently to the Income Statement:			
Currency translation on net investments		**(42)**	(346)
Share of other comprehensive income/(expense) from equity accounted investments	15	**16**	(23)
Transfer to Income Statement from equity of cumulative translation differences on disposal of foreign operations	13	**–**	(13)
Derivative losses on hedge relationships		**(99)**	(17)
Transfer to Income Statement on hedge relationships		**8**	–
Income tax credit/(charge) relating to items that may be reclassified	8	**9**	(19)
		(108)	(418)
Other comprehensive income/(expense) for the year		**78**	(435)
Total comprehensive expense for the year		**(455)**	(486)
Attributable to:			
Owners of the parent		**(458)**	(494)
Non-controlling interests		**3**	8
		(455)	(486)

Consolidated Statement of Cash Flows

	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Operating activities			
Net cash from operating activities from continuing operations	27	**768**	769
Net cash used in operating activities from discontinued operations	27	**(4)**	(20)
Net cash from operating activities		**764**	749
Investing activities			
Disposal of businesses, net of cash disposed		**10**	169
Purchase of property, plant and equipment		**(275)**	(465)
Proceeds from disposal of property, plant and equipment		**25**	24
Purchase of computer software and capitalised development costs		**(42)**	(54)
Dividends received from equity accounted investments	15	**54**	67
Purchase of investments	12	**(2)**	(50)
Settlement of derivatives used in net investment hedging		**–**	(100)
Acquisition of subsidiaries, net of cash acquired	11	**(19)**	–
Interest received		**3**	9
Net cash used in investing activities from continuing operations		**(246)**	(400)
Net cash used in investing activities from discontinued operations	27	**(2)**	(15)
Net cash used in investing activities		**(248)**	(415)
Financing activities			
Repayment of borrowings		**(598)**	(456)
New bank loans raised		**–**	350
Costs of raising debt finance		**(1)**	–
Repayment of principal under lease obligations	28	**(76)**	(70)
Dividends paid to non-controlling interests		**–**	(6)
Dividends paid to owners of the parent	9	**–**	(231)
Net cash used in financing activities from continuing operations		**(675)**	(413)
Net cash used in financing activities from discontinued operations	27	**(1)**	(2)
Net cash used in financing activities		**(676)**	(415)
Net decrease in cash and cash equivalents, net of bank overdrafts		**(160)**	(81)
Cash and cash equivalents, net of bank overdrafts at the beginning of the year	27	**317**	415
Effect of foreign exchange rate changes	27	**3**	(17)
Cash and cash equivalents, net of bank overdrafts at the end of the year	27	**160**	317

As at 31 December 2020, the Group had net debt of £2,847 million (31 December 2019: £3,283 million). A definition and reconciliation of the movement in net debt is shown in note 27.

Consolidated Balance Sheet

	Notes	31 December 2020 £m	Restated[(1)] 31 December 2019 £m	Restated[(1)] 31 December 2018 £m
Non-current assets				
Goodwill and other intangible assets	11	**9,198**	9,784	11,098
Property, plant and equipment	14	**3,133**	3,432	3,171
Investments	12	**34**	48	–
Interests in equity accounted investments	15	**430**	436	492
Deferred tax assets	22	**180**	160	132
Derivative financial assets	25	**101**	38	26
Trade and other receivables	17	**439**	424	504
		13,515	14,322	15,423
Current assets				
Inventories	16	**1,126**	1,332	1,489
Trade and other receivables	17	**1,658**	1,970	2,328
Derivative financial assets	25	**47**	19	15
Current tax assets		**23**	20	74
Cash and cash equivalents	18	**311**	512	511
Assets classified as held for sale		**–**	65	–
		3,165	3,918	4,417
Total assets	5	**16,680**	18,240	19,840
Current liabilities				
Trade and other payables	19	**2,456**	2,461	2,583
Interest-bearing loans and borrowings	20	**165**	284	473
Lease obligations	28	**81**	71	5
Derivative financial liabilities	25	**58**	106	204
Current tax liabilities		**188**	106	137
Provisions	21	**415**	412	391
Liabilities associated with assets held for sale		**–**	46	–
		3,363	3,486	3,793
Net current (liabilities)/assets		**(198)**	432	624
Non-current liabilities				
Trade and other payables	19	**421**	444	762
Interest-bearing loans and borrowings	20	**2,926**	3,464	3,378
Lease obligations	28	**474**	511	52
Derivative financial liabilities	25	**210**	216	227
Deferred tax liabilities	22	**732**	772	874
Retirement benefit obligations	24	**838**	1,121	1,413
Provisions	21	**606**	675	1,080
		6,207	7,203	7,786
Total liabilities	5	**9,570**	10,689	11,579
Net assets		**7,110**	7,551	8,261
Equity				
Issued share capital	26	**333**	333	333
Share premium account		**8,138**	8,138	8,138
Merger reserve		**109**	109	109
Other reserves		**(2,330)**	(2,330)	(2,330)
Translation and hedging reserve	26	**(30)**	78	495
Retained earnings		**861**	1,197	1,492
Equity attributable to owners of the parent		**7,081**	7,525	8,237
Non-controlling interests		**29**	26	24
Total equity		**7,110**	7,551	8,261

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

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

Geoffrey Martin

Geoffrey Martin
Group Finance Director
4 March 2021

Simon A Peckham

Simon Peckham
Chief Executive
4 March 2021

Consolidated Statement of Changes in Equity

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

Further information on issued share capital and reserves is set out in note 26.

Notes to the Financial Statements

1. Corporate information

Melrose Industries PLC ("the Company") is a public company limited by shares. The Company is incorporated in the United Kingdom under the Companies Act 2006 and registered in England and Wales. The address of the registered office is given on the back cover. The nature of the Group's operations and its principal activities by operating segment are set out in note 5 and in the Divisional reviews on pages 14 to 33. The Consolidated Financial Statements of the Group for the year ended 31 December 2020 were authorised in accordance with a resolution of the Directors of Melrose Industries PLC on 4 March 2021.

These Financial Statements are presented in pounds Sterling which is the currency of the primary economic environment in which the Company is based. Foreign operations are included in accordance with the policies set out in note 2.

Corporate structure

On 2 January 2020, the Powder Metallurgy division completed the acquisition of FORECAST 3D, a leading US specialist in plastic additive manufacturing and 3D printing services offering a full range of services from concept to series production for consideration of up to £29 million. The acquisition furthers Powder Metallurgy's ambition to achieve global market leadership in industrialising additive manufacturing. As the acquisition is not material to the Group, limited additional information is provided in note 11.

On 25 November 2020, the Group completed the disposal of the Wheels & Structures business to Aurelius Group AG, and in the prior year completed the disposal of the Walterscheid Powertrain Group. The Wheels & Structures business is shown as a discontinued operation in these Consolidated Financial Statements prior to its disposal. Further detail is shown in note 13.

Prior year restatement of cash and cash equivalents and bank overdrafts

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

1.1 New Standards, Amendments and Interpretations affecting amounts, presentation or disclosure reported in the current year

In the current financial year, the Group has adopted the following new and revised Standards, Amendments and Interpretations. Their adoption has not had a significant impact on the amounts reported in these Financial Statements:

- Amendments to IFRS 3: Definition of a business
- Amendments to IAS 1 and IAS 8: Definition of material
- Amendments to IFRS 9, IAS 39 and IFRS 7: Interest Rate Benchmark Reform
- Amendments to references to Conceptual Framework in IFRS standards
- Amendments to IFRS 16: COVID-19 related rent concessions

1.2 New Standards, Amendments and Interpretations in issue but not yet effective

At 31 December 2020, the following Standards, Amendments and Interpretations were in issue but not yet effective (and in some cases had not been adopted by the EU):

- IFRS 17: Insurance contracts
- IFRS 10 and IAS 28 (amendments): Sale or contribution of assets between an investor and an associate or joint venture
- IFRS 14: Regulatory deferral accounts
- Amendments to IAS 1: Classification of liabilities
- Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16: Interest Rate Benchmark Reform (Phase 2)

The Directors do not expect that the adoption of the above Standards, Amendments and Interpretations will have a material impact on the Financial Statements of the Group in future periods.

2. Summary of significant accounting policies

Basis of accounting

The Consolidated Financial Statements have been prepared in accordance with the requirements of the Companies Act 2006 and International Financial Reporting Standards ("IFRSs") adopted pursuant to Regulation (EC) No 1606/2002 as it applies in the European Union in addition to IFRSs as issued by the IASB. The Consolidated Financial Statements have been prepared on an historical cost basis, except for the revaluation of certain financial instruments and investments which are recognised at fair value at the end of each reporting period. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

Alternative Performance Measures

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

APMs used by the Group are set out in the glossary to these Financial Statements on pages 204 to 207 and the reconciling items between statutory and adjusted results are listed below and described in more detail in note 6.

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

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

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

- Amortisation of intangible assets that are acquired in a business combination, excluding computer software and development costs;
- Significant restructuring costs and other associated costs, including losses incurred following the announcement of closure for identified businesses, arising from significant strategy changes that are not considered by the Group to be part of the normal operating costs of the business;

2. Summary of significant accounting policies continued

- Acquisition and disposal related costs;
- Impairment charges that are considered to be significant in nature and/or value to the trading performance of the business;
- Movement in derivative financial instruments not designated in hedging relationships, including revaluation of associated financial assets and liabilities;
- Removal of adjusting items, interest and tax on equity accounted investments to reflect operating results;
- The charge for the Melrose equity-settled compensation scheme, including its associated employer's tax charge;
- Costs associated with the gender equalisation of guaranteed minimum pension ("GMP") for occupational schemes; and
- The net release of fair value items booked on acquisitions.

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

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

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

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

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

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

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

Basis of consolidation

The Group's Financial Statements include the results of the parent undertaking and all of its subsidiary undertakings. In addition, the Group's share of the results and equity of joint ventures and associated undertakings (together "equity accounted investments") are included. The results of businesses acquired during the period are included from the effective date of acquisition and, for those sold during the period, to the effective date of disposal. Where necessary, adjustments are made to the Financial Statements of subsidiaries to bring the accounting policies used into line with those used by the Group.

All intra-Group balances and transactions, including unrealised profits arising from intra-Group transactions, have been eliminated in full.

Non-controlling interests in subsidiaries are identified separately from the Group's equity therein. The interest of non-controlling shareholders is initially measured at the non-controlling interests' proportion of the share of the fair value of the acquiree's identifiable net assets. Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition plus the non-controlling interests' share of subsequent changes in equity. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Going concern

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

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

Covenants

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

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

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

Testing

The Group has modelled two scenarios in its assessment of going concern; a base case and a reasonably possible sensitised case. Please refer to note 11 for further details of the Group's forecasting considerations.

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

2. Summary of significant accounting policies continued

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

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

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

Business combinations and goodwill

The acquisition of subsidiaries is accounted for using the acquisition method. The cost of acquisition is measured at the fair value of assets transferred, the liabilities incurred or assumed at the date of exchange of control and equity instruments issued by the Group in exchange for control of the acquiree. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities. Costs directly attributable to business combinations are recognised as an expense in the Income Statement as incurred.

The acquired identifiable assets and liabilities are measured at their fair value at the date of acquisition except those where specific guidance is provided by IFRSs. Non-current assets and directly attributable liabilities that are classified as held for sale in accordance with IFRS 5: "Non-current assets held for sale and discontinued operations", are recognised and measured at fair value less costs to sell. Also, deferred tax assets and liabilities are recognised and measured in accordance with IAS 12: "Income taxes", liabilities and assets related to employee benefit arrangements are recognised and measured in accordance with IAS 19 (revised): "Employee benefits" and liabilities or equity instruments related to the replacement by the Group of an acquiree's share-based payments awards are measured in accordance with IFRS 2: "Share-based payment". Any excess of the cost of the acquisition over the fair values of the identifiable net assets acquired is recognised as goodwill.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts where appropriate. Those provisional amounts are adjusted during the measurement period, or additional assets or liabilities recognised, to reflect new information obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the amounts recognised at that date.

The measurement period is the period from the date of acquisition to the date the Group obtains complete information about facts and circumstances that existed as of the acquisition date and is subject to a maximum period of one year.

Goodwill on acquisition is initially measured at cost, being the excess of the sum of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer's previously held equity interest in the acquiree over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

If, after reassessment, the Group's interest in the fair value of the acquiree's identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the acquirer's previously held equity interest in the acquiree, the excess is recognised immediately in profit or loss as a bargain purchase gain.

As at the acquisition date, any goodwill acquired is allocated to the cash-generating units acquired. Impairment is determined by assessing the recoverable amount of the cash-generating unit to which goodwill relates. Where the recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised in the Income Statement and is not subsequently reversed. When there is a disposal of a cash-generating unit, goodwill relating to the operation disposed of is taken into account in determining the gain or loss on disposal of that operation. The amount of goodwill allocated to a partial disposal is measured on the basis of the relative values of the operation disposed of and the operation retained.

Equity accounted investments

A joint venture is an entity which is not a subsidiary undertaking but where the interest of the Group is that of a partner in a business over which the Group exercises joint control with its partners over the financial and operating policies. In all cases voting rights are 50% or lower.

Associated undertakings are entities that are neither a subsidiary nor a joint venture, but where the Group has a significant influence. The results, assets and liabilities of equity accounted investments are accounted for using the equity method of accounting. The Group's share of equity includes goodwill arising on acquisition.

When a Group entity transacts with an equity accounted investment of the Group, profits and losses resulting from the transactions with the equity accounted investments are recognised in the Group's Consolidated Financial Statements only to the extent of interests in equity accounted investments that are not related to the Group.

Notes to the Financial Statements
Continued

2. Summary of significant accounting policies continued

Revenue

Revenues are recognised either at the point of transfer of control of goods and services, or recognised over time on an activity basis using the costs incurred as the measure of the activity. Costs are recognised as they are incurred.

The nature of agreements into which the Group enters means that certain of the Group's arrangements with its customers have multiple elements that can include any combination of:

- Sale of products and services;
- Risk and revenue sharing partnerships ("RRSPs");
- Design and build; and
- Construction contracts.

Contracts are reviewed to identify each performance obligation relating to a distinct good or service and the associated consideration. The Group allocates revenue to multiple element arrangements based on the identified performance obligations within the contracts in line with the policies below. A performance obligation is identified if the customer can benefit from the good or service on its own or together with other readily available resources, and it can be separately identified within the contract. This review is performed by reference to the specific contract terms.

Sale of products and services

This revenue stream accounts for the majority of Group sales. Contracts in the Automotive, Powder Metallurgy, Nortek Air Management and Other Industrial segments operate almost exclusively on this basis, and it also covers a high proportion of the Aerospace segment's revenues.

Invoices for goods are raised and revenue is recognised when control of the goods is transferred to the customer. Dependent upon contractual terms this may be at the point of despatch, acceptance by the customer or, in Aerospace, certification by the customer. The revenue recognised is the transaction price as it is the observable selling price per product.

Cash discounts, volume rebates and other customer incentive programmes are based on certain percentages agreed with the Group's customers, which are typically earned by the customer over an annual period. These are allocated to performance obligations and are recorded as a reduction in revenue at the point of sale based on the estimated future outcome. Due to the nature of these arrangements an estimate is made based on historical results to date, estimated future results across the contract period and the contractual provisions of the customer agreement.

Many businesses in the Powder Metallurgy and Automotive segments recognise an element of revenue via a surcharge or similar raw material cost recovery mechanism. The surcharge is generally based on prior period movement in raw material price indices applied to current period deliveries.

Risk and revenue sharing partnerships ("RRSPs")

This revenue stream affects a small number of businesses, exclusively in the Aerospace segment. Revenue is recognised under RRSPs for both the sale of product as detailed above and sales of services, which are recognised by reference to the stage of completion based on the performance obligations in the contract. In most RRSP contracts, there are two separate phases where the Group earns revenue; sale of products principally to engine manufacturers and aftermarket support.

The assessment of the stage of completion is dependent on the nature of the contract and the performance obligations within it.

The value of revenue is based on the standalone selling price for each element of the contract.

Revenue is recognised at the point control passes to the customer. For products and services, this has been identified as the point of despatch, acceptance by the customer or certification by the customer. Where the amount of revenue recognised is not yet due for collection under the terms of the contract, it will be recognised as variable consideration within contract assets. Revenue is not recognised where recovery is not probable due to potential significant reversals in the future. This can be affected by assessment of future volumes including aftermarket expectations which are impacted by technology development, fuel price and competition.

Participation fees are payments made to engine manufacturers and original equipment manufacturers relating to RRSPs and long-term agreements. They are recognised as contract assets to the extent they can be recovered from future sales. Where participation fees have been paid under the RRSP, the amortisation is recognised as a revenue reduction under IFRS 15, as performance obligations are satisfied.

Generally, during the design and development phase of a typical RRSP contract, the Group performs contractually agreed-upon tasks for a customer. It is usual for the Intellectual Property Rights ("IPRs") that underpin technology advancement or know-how to remain with the Group such that the customer cannot benefit from the IPRs either on their own or together with other resources that are readily available to the customer. Where IPRs are transferred to the customer the Group has determined this is not separately identifiable from other promises in the contract due to an exclusivity clause for the supply of product. Accordingly, it has been determined that the Group's promise to transfer goods to its customer is a performance obligation that is separately identifiable and this uses development and know-how as an input.

Design and build

This revenue stream affects a discrete number of businesses, primarily in the Aerospace segment but also on a smaller scale in the Automotive segment. Generally, revenue is only recognised on the sale of product as detailed above, however, on occasions cash is received in advance of work performed to compensate the Group for costs incurred in design and development activities. The Group performs an assessment of its performance obligations to understand multiple elements. Where it is determined there is only one type of performance obligation, being the delivery of product, any cash advance is factored into the revenue allocated across the deliveries required under the contract. Where the performance obligation has not been satisfied amounts received are recognised as a contract liability. If there is more than one performance obligation, revenue is allocated to each one based on a standalone selling price for each element of the contract.

Due to the nature of design and build contracts, there can be significant 'learning curves' while the Group optimises its production processes. During the early phase of these contracts, all costs including any start-up losses are taken directly to the Income Statement, as they do not meet the criteria for fulfilment costs.

Construction contracts

Where multiple performance obligations are identified, revenue is recognised as each performance obligation is met. This requires an assessment of total revenue to identify the allocation across the performance obligations, based on the standalone selling price for each obligation.

2. Summary of significant accounting policies continued

In cases where one of the following criteria is met, revenue is recognised over time:

- The customer simultaneously receives and consumes the benefits provided by the Group's performance;
- The Group's performance creates or enhances an asset that the customer controls as the asset is created or enhanced; or
- The Group's performance does not create an asset with an alternative use to the Group and it has an enforceable right to payment for performance completed to date.

Due to the nature of the criteria above, only certain contracts in the Group qualify for over time recognition. On this basis revenue is recognised using the input method, which uses costs incurred and the assessed margin across the contract. The input method is used to measure progress as it best depicts the transfer of control to the customer. The margin and associated revenue are calculated based on the estimated transaction price and expected total costs, with considerations made for the associated contract risks.

If any of the above criteria are not met, revenue is recognised at a point in time when control transfers to the customer which, in line with the sale of goods and services above, is the point of delivery or customer acceptance dependent on the terms of the contract.

Variable consideration, such as price or scope amendments, is included based on the expected value or most likely amount. A constraint is included unless it is highly probable that the revenue will not significantly reverse in the future. This constraint is calculated based on a cautious expectation of the life of certain RRSPs and by assessing the impact of a 10% reduction in expected spares sales. Variations in contract work, claims and incentive payments are included in revenue from construction contracts based on an estimate of the expected value the Group expects to receive. Variations are included when the customer has agreed to the variation or acknowledged liability for the variation in principle. Claims are included when negotiations with the customer have reached an advanced stage such that it is virtually certain that the customer will accept the claim.

Finance income

Finance income is recognised when it is probable that the economic benefits will flow to the Group and the amount of income can be measured reliably. Finance income is accrued on a time basis, by reference to the principal outstanding and the effective interest rate applicable.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in the Income Statement in the period in which they are incurred.

Issue costs of loans

The finance cost recognised in the Income Statement in respect of the issue costs of borrowings is allocated to periods over the terms of the instrument using the effective interest rate method.

Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any impairment in value.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bring the asset into operation, and any borrowing costs on qualifying assets. Qualifying assets are defined as an asset or programme where the period of capitalisation is more than 12 months. Purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Where assets are in the course of construction at the balance sheet date, they are classified as capital work-in-progress. Transfers are made to other asset categories when they are available for use, at which point depreciation commences.

Right-of-use assets arise under IFRS 16 and are depreciated over the shorter of the estimated life and the lease term.

Depreciation is calculated on a straight-line basis over the estimated useful life of the asset as follows:

Freehold land	nil
Freehold buildings and long leasehold property	over expected economic life not exceeding 50 years
Short leasehold property	over the term of the lease
Plant and equipment	3-15 years

The estimated useful lives of property, plant and equipment are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The carrying values of property, plant and equipment are reviewed annually for indicators of impairment, or if events or changes in circumstances indicate that the carrying value may not be recoverable. If such indication exists an impairment test is performed and, where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. The recoverable amount of property, plant and equipment is the greater of net selling price and value in use. In assessing value in use, estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds or costs and the carrying amount of the item) is included in the Income Statement in the period that the item is derecognised.

2. Summary of significant accounting policies continued

Intangible assets

Intangible assets are stated at cost less accumulated amortisation and accumulated impairment losses.

On acquisition of businesses, separately identifiable intangible assets are initially recorded at their fair value at the acquisition date.

Access to the use of brands and intellectual property are valued using a "relief from royalty" method which determines the net present value of future additional cash flows arising from the use of the intangible asset.

Customer relationships and contracts are valued on the basis of the net present value of the future additional cash flows arising from customer relationships with appropriate allowance for attrition of customers.

Technology assets are valued using a replacement cost approach, or a "relief from royalty" method.

Amortisation of intangible assets is recorded in administration expenses in the Income Statement and is calculated on a straight-line basis over the estimated useful lives of the asset as follows:

Customer relationships and contracts	20 years or less
Brands and intellectual property	20 years or less
Technology	20 years or less
Computer software	5 years or less
Development costs	20 years or less

Where computer software is not integral to an item of property, plant or equipment, its costs are capitalised and categorised as intangible assets. Computer software is initially recorded at cost. Where these assets have been acquired through a business combination, this will be the fair value allocated in the acquisition accounting. Where these have been acquired other than through a business combination, the initial cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Intangible assets (other than computer software and development costs) are tested for impairment annually or more frequently whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Impairment losses are measured on a similar basis to property, plant and equipment. Useful lives are also examined on an annual basis and adjustments, where applicable, are made on a prospective basis.

Research and development costs

Research costs are expensed as incurred.

Costs relating to clearly defined and identifiable development projects are capitalised when there is a technical degree of exploitation, adequacy of resources and a potential market or development possibility in the undertaking that are recognisable; and where it is the intention to produce, market or execute the project. A correlation must also exist between the costs incurred and future benefits and those costs can be measured reliably. Capitalised costs are expensed on a straight-line basis over their useful lives of 20 years or less. Costs not meeting such criteria are expensed as incurred.

Inventories

Inventories are valued at the lower of cost and net realisable value and are measured using a first in, first out or weighted average cost basis. Cost includes all direct expenditure and appropriate production overhead expenditure incurred in bringing goods to their current state under normal operating conditions. Net realisable value is based on estimated selling price less costs expected to be incurred to completion and disposal. Provisions are made for obsolescence or other expected losses where necessary.

Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, balances with banks and similar institutions, and short-term deposits which are readily convertible to cash and are subject to insignificant risks of changes in value.

For the purpose of the Consolidated Statement of Cash Flows, cash and cash equivalents consist of cash and cash equivalents as defined above, net of outstanding bank overdrafts.

Interest-bearing loans and borrowings

All loans and borrowings are initially recognised at fair value of the consideration received net of issue costs associated with the borrowings.

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any issue costs, and any discount or premium on settlement.

Gains and losses are recognised in the Income Statement when the liabilities are derecognised or impaired, as well as through the amortisation process.

Government refundable advances

Government refundable advances are reported in "Trade and other payables" in the Balance Sheet. Refundable advances include amounts advanced by a government, accrued interest and directly attributable costs. Refundable advances are provided to the Group to part-finance expenditures on specific development programmes. The advances are provided on a risk sharing basis, i.e. repayment levels are determined subject to the success of the related programme. Balances are held at amortised cost and interest is calculated using the effective interest rate method.

Leases

Where a lease arrangement is identified, a liability to the lessor is included in the Balance Sheet as a lease obligation calculated at the present value of minimum lease payments. A corresponding right-of-use asset is recorded in property, plant and equipment. The discount rate used to calculate the lease liability is the Group's incremental borrowing rate, unless there is a rate implicit in the lease. The incremental borrowing rate is used for the majority of leases. Incremental borrowing rates are based on the term, currency, country and start date of the lease and reflect the rate the Group would pay for a loan with similar terms and security.

2. Summary of significant accounting policies continued

Following initial recognition, the lease liability is measured at amortised cost using the effective interest rate method. Where there is a change in future lease payments due to a rent review, change in index or rate, or a change in the Group's assessment of whether it is reasonably certain to exercise a purchase, extension or break option, the lease obligation is remeasured. A corresponding adjustment is made to the associated right-of-use asset.

Right-of-use assets are depreciated over the shorter of the estimated useful life of the asset and the lease term.

Lease payments are apportioned between finance costs and a reduction in the lease obligation so as to reflect the interest on the remaining balance of the obligation. Finance charges are recorded in the Income Statement within finance costs.

Leases with a term of 12 months or less and leases for low value are not recorded on the Balance Sheet and lease payments are recognised as an expense in the Income Statement on a straight-line basis over the lease term. Expenses relating to variable lease payments which are not included in the lease liability, due to being based on a variable other than an index or rate, are recognised as an expense in the Income Statement.

Financial instruments – assets

Classification and measurement

All financial assets are classified as either those which are measured at fair value, through profit or loss or Other Comprehensive Income, and those measured at amortised cost.

Financial assets are initially recognised at fair value. For those which are not subsequently measured at fair value through profit or loss, this includes directly attributable transaction costs. Trade and other receivables, contract assets and amounts due from equity accounted investments are subsequently measured at amortised cost.

Recognition and derecognition of financial assets

Financial assets are recognised in the Group's Balance Sheet when the Group becomes a party to the contractual provisions of the instrument. The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

Impairment of financial assets

For trade receivables and contract assets, the simplified approach permitted under IFRS 9 is applied. The simplified approach requires that at the point of initial recognition the expected credit loss across the life of the receivable must be recognised. As these balances do not contain a significant financing element, the simplified approach relating to expected lifetime losses is applicable under IFRS 9. Cash and cash equivalents and other receivables are also subject to impairment requirements.

Investments

The Group has an investment in unlisted shares that are not traded in an active market, but are classified as financial assets, measured at fair value. Fair value is determined by assessment of expected future dividends discounted to net present value. Any changes in fair value are recognised in Other Comprehensive Income and accumulated in retained earnings. Dividends from investments are recognised in the Income Statement when the Group's right to receive the dividend is established.

Trade and other receivables

Trade and other receivables are measured and carried at amortised cost using the effective interest method, less any impairment. For trade receivables, the carrying amount is reduced by an allowance for expected lifetime losses. Subsequent recoveries of amounts previously written off are credited against the allowance account and changes in the carrying amount of the allowance account are recognised in the Income Statement.

Trade receivables that are assessed not to be impaired individually are also assessed for impairment on a collective basis. In measuring the expected credit losses, the Group considers all reasonable and supportable information such as the Group's past experience at collecting receipts, any increase in the number of delayed receipts in the portfolio past the average credit period, and forward looking information such as forecasts of future economic decisions.

Other receivables are also considered for impairment and if required the carrying amount is reduced by any loss arising which is recorded in the Income Statement, although for the Group this is not material.

Financial instruments – liabilities

Recognition and derecognition of financial liabilities

Financial liabilities are recognised in the Group's Balance Sheet when the Group becomes a party to the contractual provisions of the instruments and are initially measured at fair value, net of transaction costs. The Group derecognises financial liabilities when the Group's obligations are discharged, significantly modified, cancelled or they expire.

Classification and measurement

Non-derivative financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective interest rate basis. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant periods. The effective interest rate is the rate that discounts estimated future cash payments throughout the expected life of the financial liability, or, where appropriate, a shorter period to the gross carrying amount of the financial liability.

Derivative financial instruments and hedging

The Group uses derivative financial instruments to manage its exposure to interest rate, foreign exchange rate and commodity risks, arising from operating and financing activities. The Group does not hold or issue derivative financial instruments for trading purposes. Details of derivative financial instruments are disclosed in note 25 of the Financial Statements.

Derivative financial instruments are recognised and stated at fair value in the Group's Balance Sheet. Their fair value is recalculated at each reporting date. The accounting treatment for the resulting gain or loss will depend on whether the derivative meets the criteria to qualify for hedge accounting and are designated as such.

Where derivatives do not meet the criteria to qualify for hedge accounting, any gains or losses on the revaluation to fair value at the period end are recognised immediately in the Income Statement. Where derivatives do meet the criteria to qualify for hedge accounting, recognition of any resulting gain or loss on revaluation depends on the nature of the hedge relationship and the item being hedged.

2. Summary of significant accounting policies continued

Derivative financial instruments with maturity dates of less than one year from the period end date are classified as current in the Balance Sheet. Derivatives embedded in non-derivative host contracts are recognised at their fair value in the Group's Balance Sheet when the nature, characteristics and risks of the derivative are not closely related to the host contract. Gains and losses arising on the remeasurement of these embedded derivatives at each balance sheet date are recognised in the Income Statement.

Hedge accounting

In order to qualify for hedge accounting, the Group is required to document from inception the relationship between the item being hedged and the hedging instrument, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents that the hedge will be highly effective, which is when the hedging relationships meet all of the following hedge effectiveness requirements:

- there is an economic relationship between the hedged item and the hedging instrument;
- the effect of credit risk does not dominate the value changes that result from that economic relationship; and
- the hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group actually uses to hedge that quantity of hedged item.

The Group discontinues hedge accounting only when the hedging relationship (or a part thereof) ceases to meet the qualifying criteria (after rebalancing, if applicable). This includes instances when the hedging instrument expires or is sold, terminated or exercised. The discontinuation is accounted for prospectively.

The Group designates certain hedging instruments as either cash flow hedges or hedges of net investments in foreign operations.

Cash flow hedge

Derivative financial instruments are classified as cash flow hedges when they hedge the Group's exposure to the variability in cash flows that are either attributable to a particular risk associated with a recognised asset or liability, or a highly probable forecasted cash flow.

The Group designates the full change in the fair value of a foreign exchange forward contract (i.e. including the forward elements) as the hedging instrument for all of its hedging relationships involving foreign exchange forward contracts.

The effective portion of any gain or loss from revaluing the derivative financial instrument is recognised in the Statement of Comprehensive Income and accumulated in equity. The gain or loss relating to the ineffective portion is recognised immediately in the Income Statement.

Amounts previously recognised in the Statement of Comprehensive Income and accumulated in equity are recycled to the Income Statement in the periods when the hedged item is recognised in the Income Statement or when the forecast transaction is no longer expected to occur. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the non-financial asset or non-financial liability.

Hedges of net investments in foreign operations

Derivative financial instruments are classified as net investment hedges when they hedge the Group's net investment in foreign operations. The effective element of any foreign exchange gain or loss from revaluing the derivative at a reporting period end is recognised in the Statement of Comprehensive Income. Any ineffective element is recognised immediately in the Income Statement.

The Group designates only the spot rate component of cross currency swaps in net investment hedges. The changes in the fair value of the aligned forward and currency basis elements are recognised in other comprehensive income and accumulated in equity. If the hedged item is time-period related, then the amount accumulated in equity is reclassified to profit or loss on an appropriate basis.

Gains and losses accumulated in equity are recognised immediately in the Income Statement when the foreign operation is disposed.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a rate that reflects the current market assessment of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

Contingent liabilities acquired in a business combination

Contingent liabilities acquired in a business combination are initially measured at fair value at the acquisition date. At the end of subsequent reporting periods, such contingent liabilities are measured at the higher of the amount that would be recognised in accordance with IAS 37: "Provisions, contingent liabilities and contingent assets" and the amount initially recognised less cumulative amount of revenue recognised in accordance with the principles of IFRS 15: "Revenue from contracts with customers".

Pensions and other retirement benefits

The Group operates defined benefit pension plans and defined contribution plans, some of which require contributions to be made to administered funds separate from the Group.

For the defined benefit pension and retirement benefit plans, plan assets are measured at fair value and plan liabilities are measured on an actuarial basis and discounted at an interest rate equivalent to the current rate of return on a high quality corporate bond of equivalent currency and term to the plan liabilities. Any assets resulting from this calculation are limited to past service cost plus the present value of available refunds and reductions in future contributions to the plan. The present value of the defined benefit obligation, and the related current service cost and past service cost, are measured using the projected unit credit method.

The service cost of providing pension and other retirement benefits to employees for the period is charged to the Income Statement.

Net interest expense on net defined benefit obligations is determined by applying discount rates used to measure defined benefit obligations at the beginning of the year to net defined benefit obligations at the beginning of the year. The net interest expense is recognised within finance costs.

Remeasurement gains and losses comprise actuarial gains and losses, the effect of the asset ceiling (if applicable) and the return on plan assets (excluding interest). Remeasurement gains and losses, and taxation thereon, are recognised in full in the Statement of Comprehensive Income in the period in which they occur and are not subsequently recycled.

2. Summary of significant accounting policies continued

Actuarial gains and losses may result from differences between the actuarial assumptions underlying the plan obligations and actual experience during the period or changes in the actuarial assumptions used in the valuation of the plan obligations.

For defined contribution plans, contributions payable are charged to the Income Statement as an operating expense when employees have rendered services entitling them to the contributions.

Foreign currencies

The individual Financial Statements of each Group company are presented in the currency of the primary economic environment in which it operates (its functional currency). For the purpose of the Consolidated Financial Statements, the results and financial position of each Group company are expressed in pounds Sterling, which is the functional currency of the Company, and the presentation currency for the Consolidated Financial Statements.

In preparing the Financial Statements of the individual companies, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in the Income Statement for the period. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in the Income Statement for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognised directly in equity.

For the purpose of presenting Consolidated Financial Statements, the assets and liabilities of the Group's foreign operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used. Exchange differences arising, if any, are recognised in the Statement of Comprehensive Income and accumulated in equity (attributed to non-controlling interests as appropriate). Such translation differences are recognised as income or as expenses in the period in which the related operation is disposed of. Any exchange differences that have previously been attributed to non-controlling interests are derecognised but they are not reclassified to the Income Statement.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the rate prevailing at the balance sheet date.

Taxation

The tax expense is based on the taxable profits for the period and represents the sum of the tax paid or currently payable and deferred tax.

Taxable profit differs from net profit as reported in the Income Statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.

A tax provision is recognised for those matters for which the tax determination is uncertain but it is considered probable that there will be a future outflow of funds to a tax authority. The provisions are measured at the best estimate of the amount expected to become payable. The assessment is based on the judgement of tax professionals within the Company supported by previous experience in respect of such activities and in certain cases based on specialist independent advice.

Deferred tax is provided, using the liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognised for all taxable temporary differences except:

- where the deferred tax liability arises on the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- where the timing of the reversal of the temporary differences associated with investments in subsidiaries and interests in equity accounted investments can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carry-forward of unused tax assets and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and carry-forward of unused tax assets and unused tax losses can be utilised except:

- where the deferred tax asset arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries and interests in equity accounted investments, deferred tax assets are only recognised to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the relevant balance sheet date.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Tax relating to items recognised directly in other comprehensive income is recognised in the Statement of Comprehensive Income and not in the Income Statement.

2. Summary of significant accounting policies continued

Revenues, expenses and assets are recognised net of the amount of sales tax except:

- where the sales tax incurred on a purchase of goods and services is not recoverable from the taxation authority, in which case the sales tax is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- where receivables and payables are stated with the amount of sales tax included.

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the Balance Sheet.

Share-based payments

The Group has applied the requirements of IFRS 2: "Share-based payment". The Group issues equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value of the equity instrument excluding the effect of non-market based vesting conditions at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest and adjusted for the effect of non-market based vesting conditions.

Fair value is measured by use of the Black-Scholes pricing model. The expected life used in the model has been adjusted, based on the Directors' best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

Non-current assets and disposal groups

Non-current assets and businesses classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell. Non-current assets and businesses are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as having been met only when the sale is highly probable and the asset or business is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

3. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in note 2, the Directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experiences and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of revision and future periods if the revision affects both current and future periods.

Critical judgements

In the course of preparing the Financial Statements, a critical judgement within the scope of paragraph 122 of IAS 1: "Presentation of Financial Statements" is made during the process of applying the Group's accounting policies.

Adjusting items

Judgements are required as to whether items are disclosed as adjusting, with consideration given to both quantitative and qualitative factors. Further information about the determination of adjusting items in the year ended 31 December 2020 is included in note 2.

There are no other critical judgements other than those involving estimates, that have had a significant effect on the amounts recognised in the Financial Statements. Those involving estimates are set out below.

Key sources of estimation uncertainty

Assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that may have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

a) Assumptions used to determine the recoverable amount of goodwill and other assets

The carrying value of goodwill in the Group at 31 December 2020 was £3,640 million (31 December 2019: £3,653 million).

Determining whether goodwill of groups of cash generating units ("CGUs") is impaired requires an estimation of its recoverable amount which is compared against the carrying value. Recoverable amount is deemed to be the higher of the value in use and fair value less costs to sell. The value in use calculation requires the Directors to estimate the future cash flows expected to arise from the groups of CGUs and a suitable discount rate in order to calculate present value. The fair values of the groups of CGUs are calculated using a combination of estimated discounted cash flows and EBITDA multiples, as in the current environment it has been difficult to assess a sales value using observable market inputs (level 1) or inputs based on market evidence (level 2) and so unobservable inputs (level 3) have been used.

Due to the impact of COVID-19, as explained in note 11, certain of the groups of CGUs are sensitive to changes in estimates:

Carrying amount of goodwill and other intangible assets (not including computer software and development costs)	31 December 2020 £m	31 December 2019 £m
Nortek Control (formerly Security & Smart Technology)	276	297
Ergotron	534	566
Aerostructures	1,625	1,722
Aerospace Engine Systems	2,110	2,295
Aerospace	3,735	4,017
Automotive Driveline	1,348	1,407
Automotive ePowertrain	824	913
Automotive	2,172	2,320
Powder Metallurgy	1,152	1,156

3. Critical accounting judgements and key sources of estimation uncertainty continued

Certain groups of CGUs are more at risk than others and this could possibly lead to an impairment or loss on disposal in the next year, depending on how markets continue to recover from the COVID-19 implications. The sensitivity disclosures in note 11 show reasonably possible changes to key assumptions and their effect on the impairment models, which could reduce headroom to nil. In order for a material impairment to be recorded the following, which are also reasonably possible changes in key assumptions, would need to change as set out below:

- In the Aerospace groups of CGUs, terminal operating profit would need to reduce by 15% which would reduce the terminal operating margin by 1.6 percentage points, or revenue reduce by 17%.
- In the Automotive groups of CGUs, terminal operating profit would need to reduce by 16% which would reduce the terminal operating margin by 1.8 percentage points.
- In the Powder Metallurgy groups of CGUs, terminal operating profit would need to reduce by 16% which would reduce the terminal operating margin by 2.2 percentage points.
- In the Nortek Control groups of CGUs, terminal operating profit would need to reduce by 39% which would reduce the terminal operating margin by 4.1 percentage points.
- In the Ergotron groups of CGUs, terminal operating profit would need to reduce by 4% which would reduce the terminal operating margin by 1.0 percentage points.

b) Assumptions used to determine the carrying amount of the Group's retirement benefit obligations

The Group's pension plans are significant in size. The defined benefit obligations in respect of the plans are discounted at rates set by reference to market yields on high quality corporate bonds. Significant estimation is required when setting the criteria for bonds to be included in the population from which the yield curve is derived. The most significant criteria considered for the selection of bonds to include are the issue size of the corporate bonds, quality of the bonds and the identification of outliers which are excluded. In addition, assumptions are made in determining mortality and inflation rates to be used when valuing the plan's defined benefit obligations. At 31 December 2020, the retirement benefit obligation was a deficit of £838 million (31 December 2019: £1,121 million).

Further details of the assumptions applied and a sensitivity analysis on the principal assumptions used to determine the defined benefit liabilities of the Group's obligations are shown in note 24. Whilst actual movements might be different to sensitivities shown, these are a reasonably possible change that could occur.

c) Loss-making contracts

Loss-making contract provisions represent the forecast unavoidable costs required to meet the obligations of long-term agreements, in excess of the contractual inflow expected to be generated in respect of these agreements. In assessing the unavoidable costs, management has considered the possibility that future actions could impact the profitability of the contracts. Calculation of the liability includes estimations of volumes, price and costs to be incurred over the life of the contract, which are discounted to a current value. Future changes within these estimates, or commercial progress could have a material impact on the provision in future periods. At 31 December 2020, the carrying value of the loss-making contract provision in the Group was £241 million (31 December 2019: £384 million). In the last two years significant progress has been made resolving commercial and operational issues within a large number of loss-making contracts inherited on acquisition of GKN. The release has on average been 27% of the balance immediately before reassessment. If the Group were to achieve a similar level of success on the amount outstanding at 31 December 2020, there could be a further £65 million released to adjusting items in the next year.

d) Inventory provisioning

The calculation of inventory provisions requires judgement by management of the expected value of future sales. If the carrying value of inventory is higher than the expected recoverable value, the Group makes provisions writing inventory down to its net recoverable value. The inventory is initially assessed for impairment by comparing inventory levels to recent utilisation rates and carrying values to historical selling prices. A detailed review is completed for inventory lines identified in the initial assessment considering sales activity, order flow, customer contracts and current selling price.

At 31 December 2020, there were provisions of £351 million (31 December 2019: £292 million) against gross inventory of £1,477 million (31 December 2019: £1,624 million). During the year ended 31 December 2020, the increase in inventory provisions has been significantly impacted by the global implications of COVID-19. The provision as a proportion of gross inventory has increased from 18% to 24%. If commercial and market conditions change such that just half of this movement occurs in the next year to a stable gross balance, the Group could see a further change to inventory provisions of £44 million.

e) Estimates of future revenues and costs of long-term contractual arrangements

The Group has certain large, complex contracts where significant judgements and estimates are required in order to identify the performance obligations and associated consideration.

A key judgement is the recognition and measurement of variable consideration, in particular relating to risk and revenue sharing partnerships ("RRSPs"). A detailed review of the Group's RRSP contracts determined where terms and conditions result in variable consideration and this is further set out in note 17. Distinguishing between a contractual right and the economic compulsion of partners with regard to the sale of original equipment ("OE") components and aftermarket activities relies on an interpretation of complex legal agreements. This specific point governs whether variable consideration is recognised on the sale of OE components and this can significantly impact the level of profitability from one period to the next. Further disclosure is set out in note 4.

The forecast revenues and costs in respect of RRSP contracts are inherently imprecise and significant estimates are required to assess the pattern of future maintenance activity, the costs to be incurred and escalation of revenue and costs. The estimates take account of the uncertainties, constraining the expected level of revenue as appropriate. Measurement of variable consideration is driven by forecasting aftermarket revenue per delivered engine which is in turn contingent on overall programme success, levels of discounting that might be offered by the engine manufacturers (the Group's customers), engineering requirements needed for optimal performance of the engine and the allocation of revenue to individual units. In addition, where programmes are at an early stage the wider implications of any competing engines as well as complications outside of the Group can be difficult to assess. Any of these inputs could change in the next year as programmes evolve and due to the size and scale of these contracts, almost any modification could result in material changes in future periods.

3. Critical accounting judgements and key sources of estimation uncertainty continued

The variable consideration contract asset calculated is the best estimate of revenue allocated to completed performance obligations using input assumptions and constraints as detailed further in note 17. A reasonably possible change in assumptions, such as engineering requirements to support programmes and the expected life of certain engines could have led to the variable consideration asset on the Balance Sheet of £247 million (2019: £242 million) increasing to between £261 million and £264 million. This could lead to recognition of additional profit in the year of between £14 million and £17 million.

4. Revenue

An analysis of the Group's revenue is as follows:

Continuing operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue recognised at a point in time	7,600	9,751
Revenue recognised over time	1,170	1,216
Revenue	**8,770**	10,967

As set out in the accounting policies in note 2, the Group has four primary revenue streams. There is little judgement or estimation in the revenue recognition of three of these areas; (i) sale of products and services, (ii) design and build and (iii) construction contracts. However, in the fourth area, as disclosed in note 3e, there is estimation involved in accounting for certain RRSP contracts, which arise exclusively in the Aerospace business. RRSP contracts generally include the sale of products and services as well as certain aspects of design and build arrangements. Further details are set out below.

Risk and revenue sharing partnerships

The Group has approximately £9 billion (2019: £9 billion) in respect of contractual transaction prices including a constrained estimate of variable consideration, on four engine programmes, out of a wider population of such programmes, which has been allocated to contracted performance obligations not satisfied at 31 December 2020. These performance obligations will be satisfied and revenue will be recognised over a period of up to 28 years (2019: 29 years).

The amount of revenue recognised from RRSP contracts during the year was £354 million, which includes variable consideration of £13 million (2019: £679 million, which included variable consideration of £45 million). Within this there is revenue from the delivery of product which is recognised at a point in time of £326 million (2019: £637 million) and revenue from provision of service which is recognised over time of £28 million (2019: £42 million). Due to the nature of certain of these RRSP arrangements, there is associated variable consideration and the contract asset, including movements during the year, is disclosed in note 17.

The nature of products and services delivered in RRSP contracts varies depending on the individual terms. Typically, they include a design and development phase (which has been determined not to be a distinct performance obligation and so no revenue is recognised) and two other phases where the Group does have performance obligations and earns revenue:

i) Sale of structural OE engine components, such as turbine cases, principally to engine manufacturers, where revenue is recognised at a point in time; and

ii) Aftermarket support which can include: sale of spare parts where revenue is recognised at a point in time and stand ready services for life of engine obligations to maintain permanent technical, and other programme related, support functions. Obligations can occur at any time during the engine life and include; engineering and technical support for engine configuration changes and provision of aftermarket inventory support solutions.

RRSP revenue recognised over time

The nature of these RRSP contracts on long-term engine programmes means that, as a partner, the Aerospace business can share revenue earned from maintenance, repair and overhaul services which are provided by the engine manufacturers (the Group's customers) or their sub-contractors, but not the Group. The Group has a stand ready obligation to contribute to certain of the partnerships which typically results in the provision of services such as technical and other programme support activities over the whole life of the engine. These services occur over the life of the engine and due to the nature of compensation from customer arrangements, which is often flight hour based, as well as costs which are less predictable, revenue is recognised over time using the engine manufacturer's actual overhaul costs as an input method. This method is considered appropriate as it best reflects the customers' receipt and consumption of benefit from the Group's stand ready performance obligation.

The total contract revenue includes amounts from: expected sales of OE engine components, expected sales of spare parts and aftermarket revenue per delivered engine for stand ready services for the life of engine obligations. The total contract revenue is allocated to all of the performance obligations.

During the year £nil (2019: £3 million) of revenue has been recognised relating to performance obligations satisfied by the Group in the previous year, as risks have been reduced and the constraint reassessed. In 2019 there was an additional £7 million of revenue recognised from changes in assumptions following operational progress with customers.

5. Segment information

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

The operating segments are as follows:

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

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

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

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

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

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

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

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

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

a) Segment revenues

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

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

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

5. Segment information continued

b) Segment operating profit

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

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

(1) Further details on adjusting items are discussed in note 6.
(2) Corporate adjusted operating loss of £46 million (2019: £52 million), includes £12 million (2019: £20 million) of costs in respect of divisional long-term incentive plans.

5. Segment information continued

c) Segment total assets and liabilities

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

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

d) Segment capital expenditure and depreciation

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

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

e) Geographical information

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

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

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

(1) Revenue is presented by destination.

6. Reconciliation of adjusted profit measures

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

a) Operating profit

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

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

b. Restructuring and other associated costs in the year totalling £220 million (2019: £238 million) are shown as adjusting items due to their size and non-trading nature. During the year ended 31 December 2020 these included:
- A charge of £110 million (2019: £79 million) within the Aerospace division primarily relating to costs incurred globally to reduce the business's headcount and cost structure in reaction to the significant impact that COVID-19 is having on the aerospace industry. This charge also included costs in respect of the continuation of the business's global integration, announced last year, to create "One Aerospace", ensuring the business is well positioned and able to react to changes in its new environment; and the continuation of costs relating to rationalisation projects commenced in the previous year.
- A charge of £60 million (2019: £83 million) within the Automotive division, as the business has accelerated its efforts to address its high cost base, inherited on acquisition, and best position itself as it recovers post COVID-19.
- A charge of £48 million (2019: £19 million) within the Powder Metallurgy division including costs associated with realigning the business for future demand, along with consolidation actions started in 2019 and the commencement during 2020 of the closure of a site in its underperforming North American Structural business.
- A net charge of £2 million (2019: £57 million) within the Nortek Air Management, Other Industrial and Corporate divisions which includes the completion of a factory consolidation within the HVAC business; the finalisation of the changes made in the Nortek Control business to move to a third party contract manufacturing model; and the profit from the disposal of a Dutch property held within the Brush business left vacant following the factory consolidation programme commenced in 2018.

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

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

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

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

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

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

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

6. Reconciliation of adjusted profit measures continued

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

b) Profit before tax

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

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

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

c) Profit after tax

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

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

7. Expenses

Continuing operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Net operating expenses comprise:		
Selling and distribution costs	**(177)**	(224)
Administration expenses(1)	**(1,471)**	(1,731)
Total net operating expenses	**(1,648)**	(1,955)

(1) Includes £648 million (2019: £756 million) of adjusting items (note 6).

Continuing operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Operating (loss)/profit is stated after charging/(crediting):		
Cost of inventories	**7,492**	8,732
Amortisation of intangible assets acquired in business combinations	**526**	534
Depreciation and impairment of property, plant and equipment	**596**	448
Impairment of goodwill	**–**	179
Amortisation and impairment of computer software and development costs	**75**	64
Lease expense(1)	**5**	3
Staff costs	**2,434**	2,868
Research and development costs(2)	**248**	283
Profit on disposal of property, plant and equipment	**(6)**	(6)
Expense of writing down inventory to net realisable value	**163**	66
Reversals of previous write-downs of inventory	**(65)**	(38)
Impairment recognised on trade receivables	**18**	21
Impairment reversed on trade receivables	**(17)**	(6)

(1) Includes costs relating to short-term leases of £3 million (2019: £2 million), low value leases of £1 million (2019: £1 million) and variable lease payments not included in lease liabilities of £1 million (2019: £nil).
(2) Includes staff costs totalling £175 million (2019: £195 million).

Notes to the Financial Statements
Continued

7. Expenses continued
The analysis of auditor's remuneration is as follows:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Fees payable to the Company's auditor for the audit of the Company's annual accounts	**7.7**	7.6
Fees payable to the Company's auditor and their associates for other audit services to the Group:		
The audit of the Company's subsidiaries pursuant to legislation	**1.2**	1.1
Total audit fees	**8.9**	8.7
Audit-related assurance services:		
Review of the half year interim statement	**0.4**	0.4
Non-statutory audit of certain of the Company's businesses	**1.6**	0.4
Other assurance services	**0.4**	–
Total audit-related assurance services	**2.4**	0.8
Total audit and audit-related assurance services	**11.3**	9.5
Tax compliance services	**–**	0.1
Other tax advisory services	**–**	0.1
Total audit and non-audit fees	**11.3**	9.7

Details of the Company's policy on the use of the auditors for non-audit services and how auditor's independence and objectivity were safeguarded are set out in the Audit Committee report on page 106 to 107. No services were provided pursuant to contingent fee arrangements.

An analysis of staff costs and employee numbers is as follows:

Continuing operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Staff costs during the year (including executive Directors)		
Wages and salaries(1)	**2,004**	2,373
Social security costs(2)	**335**	388
Pension costs (note 24)		
– defined benefit plans(3)	**12**	8
– defined contribution plans	**69**	86
Share-based compensation expense(4) (note 23)	**14**	13
Total staff costs	**2,434**	2,868

(1) Net of amounts received of £91 million (2019: £nil) as a result of global government assistance schemes during the COVID-19 pandemic. All amounts received from the UK government have been repaid during the year.
(2) Includes an employer's tax credit of £3 million (2019: charge of £4 million) on the change in value of the employee share plans, shown as an adjusting item (note 6).
(3) Includes a past service cost of £2 million (2019: £nil) in respect of GMP equalisation, shown as an adjusting item (note 6).
(4) Shown as an adjusting item (note 6).

Continuing operations	Year ended 31 December 2020 Number	Year ended 31 December 2019 Number
Average monthly number of persons employed (including executive Directors)		
Aerospace	**16,402**	17,050
Automotive	**20,040**	22,596
Powder Metallurgy	**6,433**	6,934
Nortek Air Management	**5,495**	5,571
Other Industrial	**2,975**	3,894
Corporate	**50**	47
Total average number of persons employed	**51,395**	56,092

7. Expenses continued
An analysis of finance costs and income is as follows:

Continuing operations	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Finance costs and income		
Interest on bank loans and overdrafts	**(136)**	(152)
Amortisation of costs of raising finance(1)	**(20)**	(11)
Net interest cost on pensions	**(19)**	(31)
Lease interest	**(21)**	(21)
Unwind of discount on provisions	**(2)**	(7)
Fair value changes on cross-currency swaps(2)	**(2)**	1
Total finance costs	**(200)**	(221)
Finance income	**3**	9
Total net finance costs	**(197)**	(212)

(1) Includes £8 million (2019: £nil) in respect of bank facility negotiation fees. These costs are shown as adjusting items (note 6).
(2) These costs are shown as adjusting items (note 6).

8. Tax

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

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

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

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

8. Tax continued

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

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
(Loss)/profit before tax:		
Continuing operations	(535)	106
Discontinued operations (note 13)	–	(82)
	(535)	24
Tax (credit)/charge on (loss)/profit before tax at the weighted average rate of 27.0% (2019: 21.0%)	(144)	5
Tax effect of:		
Disallowable expenses and other permanent differences within adjusted profit	–	6
Disallowable items included within adjusting items	3	54
Temporary differences not recognised in deferred tax	65	17
Recognition of previously unrecognised deferred tax assets	–	(16)
Tax credits, withholding taxes and other rate differences	6	4
Adjustments in respect of prior years	(12)	(5)
Tax charge/(credit) classified within adjusting items	78	(9)
Effect of changes in tax rates	(6)	(2)
Total tax (credit)/charge for the year	(10)	54

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

Tax charges included in Other Comprehensive Income are as follows:

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

Franked investment income – litigation

Since 2003, the GKN group has been involved in litigation with HMRC in respect of various advance corporate tax payments and corporate tax paid on certain foreign dividends which, in its view, were levied by HMRC in breach of the Group's EU community law rights. The most recent Supreme Court judgment in the case was published in November 2020. The Supreme Court referred back to the High Court the question of the relevant time limit for claims. Detailed technical points were heard by the Supreme Court in October 2020. The judgment on these matters has not yet been delivered and, accordingly, significant uncertainty over the future outcome remains.

The continuing complexity of the case and uncertainty over the issues raised (and in particular the timetable issue referred back to the High Court) means that it is not possible to predict the final outcome of the litigation with any reasonable degree of certainty.

9. Dividends

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

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

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

10. Earnings per share

Earnings attributable to owners of the parent	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Earnings for basis of earnings per share	(536)	(60)
Less: loss for the year from discontinued operations (note 13)	10	106
Earnings for basis of earnings per share from continuing operations	(526)	46

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

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

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

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

Adjusted earnings per share from continuing operations

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

Notes to the Financial Statements

Continued

11. Goodwill and other intangible assets

	Goodwill £m	Customer relationships and contracts £m	Brands and intellectual property £m	Other[1] £m	Computer software £m	Development costs £m	Total £m
Cost							
At 1 January 2019	4,277	5,226	871	1,057	53	496	11,980
Additions	–	–	–	–	6	48	54
Transfer to held for sale[2]	–	(10)	(8)	(3)	(2)	–	(23)
Disposal of businesses[3]	(92)	(65)	(68)	–	(5)	–	(230)
Disposals	–	–	–	–	(1)	(1)	(2)
Exchange adjustments	(147)	(190)	(19)	(17)	(3)	(30)	(406)
At 31 December 2019	4,038	4,961	776	1,037	48	513	11,373
Additions	–	–	–	–	17	25	42
Acquisition of businesses[4]	15	10	–	9	–	–	34
Disposals	–	–	–	–	(5)	(8)	(13)
Exchange adjustments	(30)	(55)	–	(1)	(1)	(1)	(88)
At 31 December 2020	**4,023**	**4,916**	**776**	**1,045**	**59**	**529**	**11,348**
Amortisation and impairment							
At 1 January 2019	(219)	(372)	(124)	(98)	(22)	(47)	(882)
Charge for the year:							
Adjusted operating profit	–	–	–	–	(12)	(52)	(64)
Adjusting items	–	(383)	(48)	(109)	–	–	(540)
Impairments[5]	(179)	–	–	–	–	–	(179)
Transfer to held for sale[2]	–	1	1	1	2	–	5
Disposal of businesses[3]	–	5	11	–	4	–	20
Disposals	–	–	–	–	1	1	2
Exchange adjustments	13	23	4	3	4	2	49
At 31 December 2019	(385)	(726)	(156)	(203)	(23)	(96)	(1,589)
Charge for the year:							
Adjusted operating profit	–	–	–	–	(13)	(44)	(57)
Adjusting items	–	(379)	(43)	(104)	–	–	(526)
Impairments[5]	–	–	–	–	(1)	(17)	(18)
Disposals	–	–	–	–	5	8	13
Exchange adjustments	2	22	1	1	1	–	27
At 31 December 2020	**(383)**	**(1,083)**	**(198)**	**(306)**	**(31)**	**(149)**	**(2,150)**
Net book value							
At 31 December 2020	**3,640**	**3,833**	**578**	**739**	**28**	**380**	**9,198**
At 31 December 2019	3,653	4,235	620	834	25	417	9,784

(1) Other includes technology and order backlog intangible assets recognised on acquisitions.
(2) Transfers to held for sale in 2019 related to the Wheels & Structures business, which is shown as a discontinued operation, and was subsequently disposed of in 2020 (note 13).
(3) Disposal of businesses in 2019 related to the sale of the Walterscheid Powertrain Group.
(4) Acquisition of businesses in 2020 relates to the purchase of FORECAST 3D in the Powder Metallurgy division.
(5) The impairment charge in 2020 primarily relates to development costs written off as a result of the COVID-19 pandemic, and in 2019 related to goodwill in Nortek Control. These are shown as adjusting items within impairment of assets (note 6).

On 2 January 2020, Powder Metallurgy completed the acquisition of FORECAST 3D, a leading US specialist in plastic additive manufacturing and 3D printing services, offering a full range of services from concept to series production, for a total consideration of up to £29 million. A total of £19 million was paid in cash on 2 January 2020. The fair value allocation has been finalised.

The goodwill generated as a result of major acquisitions represents the premium paid in excess of the fair value of all net assets, including intangible assets, identified at the point of acquisition. The carrying value of goodwill includes a premium, paid in order to secure shareholder agreement to the business combination, that is less than the value that the Directors believed could be added to the acquired businesses through the application of their specialist turnaround experience.

The goodwill arising on bolt-on acquisitions is attributable to the anticipated profitability and cash flows arising from the businesses acquired, synergies as a result of the complementary nature of the business with existing Melrose businesses, the assembled workforce, technical expertise, knowhow, market share and geographical advantages afforded to the Group.

The future improvements applied to the acquired businesses, achieved through a combination of revised strategic direction, operational improvements and investment, are expected to result in improved profitability of the acquired businesses during the period of ownership and are also expected to result in enhanced disposal proceeds when the acquired businesses are ultimately disposed. The combined value achieved from these improvements is expected to be in excess of the value of goodwill acquired.

11. Goodwill and other intangible assets continued

Goodwill acquired in business combinations, net of impairment, has been allocated to the businesses, each of which comprises several cash-generating units ("CGUs"). The goodwill is tested annually for impairment, or as required if indicators of impairment are identified. Effective from the year ended 31 December 2020, the date of the annual impairment test has been moved to 31 October to better align with internal forecasting and review processes. The key assumptions used in the 31 October impairment testing were reassessed at 31 December, however, there were no further indicators of value decline that necessitated further consideration.

Following the Aerospace reorganisation, announced on 3 September 2019, the Aerostructures, Aerospace Engine Systems and Aerospace Special Technologies groups of CGUs were reorganised into the Aerospace Engine Systems and Aerostructures groups of CGUs effective 1 January 2020. As a consequence of COVID-19 and subsequent further rationalisations, the Aerostructures and Aerospace Engine Systems groups of CGUs were reorganised into one Aerospace group of CGUs. Also due to business changes resulting from the COVID-19 global pandemic, the Automotive Driveline and Automotive ePowertrain groups of CGUs were reorganised into one Automotive group of CGUs. Both of these reorganisations were effective from 1 November 2020.

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

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

Impairment testing

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

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

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

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

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

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

Notes to the Financial Statements
Continued

11. Goodwill and other intangible assets continued

Significant assumptions and estimates

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

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

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

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

Risk adjusted discount rates

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

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

Assumptions applied in financial forecasts

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

Revenue growth and operating margins:

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

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

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

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

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

11. Goodwill and other intangible assets continued

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

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

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

Long-term growth rates:

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

Sensitivity analysis impacting certain groups of CGUs

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

Aerostructures group of CGUs – sensitivity analysis

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

Aerospace Engine Systems group of CGUs – sensitivity analysis

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

Powder Metallurgy group of CGUs – sensitivity analysis

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

Automotive Driveline group of CGUs – sensitivity analysis

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

Automotive ePowertrain group of CGUs – sensitivity analysis

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

Nortek Control – sensitivity analysis

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

Ergotron – sensitivity analysis

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

Notes to the Financial Statements
Continued

11. Goodwill and other intangible assets continued

Allocation of significant intangible assets

The allocation of significant customer relationships, brands, intellectual property and technology is as follows:

	Customer relationships				Brands, intellectual property and technology			
	Remaining amortisation period		Net book value		Remaining amortisation period		Net book value	
	31 December 2020 years	31 December 2019 years	**31 December 2020 £m**	31 December 2019 £m	**31 December 2020 years**	31 December 2019 years	**31 December 2020 £m**	31 December 2019 £m
Brush	**–**	–	**–**	–	**8**	9	**44**	48
AQH	**10**	11	**137**	155	**11**	12	**43**	49
HVAC	**7**	8	**66**	79	**11**	12	**56**	63
Nortek Control	**10**	11	**83**	95	**11**	12	**26**	30
Ergotron	**6**	7	**61**	74	**14**	15	**67**	74
Aerostructures(1)	**8**	9	**544**	604	**18**	19	**476**	523
Aerospace Engine Systems	**18**	19	**1,601**	1,761	**18**	19	**172**	188
Aerospace			**2,145**	2,365			**648**	711
Automotive Driveline	**10**	11	**549**	604	**18**	19	**109**	115
Automotive ePowertrain	**7**	8	**241**	285	**18**	19	**247**	289
Automotive			**790**	889			**356**	404
Powder Metallurgy	**15**	16	**551**	578	**18**	19	**77**	75
			3,833	4,235			**1,317**	1,454

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

12. Investments

Investments, carried at fair value	31 December 2020 £m	31 December 2019 £m
Shares	**34**	48

The investment in shares represents the Group's 4% investment in PW1100G-JM Engine Leasing LLC, an engine leasing business. The Group paid £50 million for this investment in 2019 and an additional £2 million in the year ended 31 December 2020. There was a loss on remeasurement to fair value of £16 million (2019: £nil) and a foreign exchange translation loss of £nil (2019: £2 million). A dividend of £4 million (2019: £nil) was received during the year which was recorded in operating profit.

This investment is classified as a level 3 fair value under the IFRS 13 fair value hierarchy. To calculate the value at 31 December 2020, the expected dividend flow was discounted to net present value using a discount rate of 9.5%. If the discount rate changed from 9.5% to 8.5% the fair value would have changed to £37 million.

13. Assets held for sale and discontinued operations

Wheels & Structures

On 28 April 2020, the Group disposed of two Chinese entities from the Wheels & Structures business for cash consideration of £8 million and recognised a loss on disposal of £6 million. On 25 November 2020, the remainder of the Wheels & Structures business was disposed for cash consideration of £13 million, realising no gain or loss on disposal. In addition, the costs charged to the Income Statement associated with the two disposals totalled £2 million and an amount of £nil was recycled from the translation and hedging reserve on disposal. Total cash disposed was £3 million. This business was held for sale as at 31 December 2019.

On 25 June 2019, the Group completed the sale of the Walterscheid Powertrain Group for cash consideration of £185 million. The costs charged to the Income Statement associated with the disposal were £7 million. The loss on disposal was £21 million after the recycling of a net favourable cumulative translation difference of £13 million.

Financial performance of discontinued operations:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue	**144**	423
Operating costs(1)	**(144)**	(503)
Operating loss	**–**	(80)
Finance costs	**–**	(2)
Loss before tax	**–**	(82)
Tax	**(2)**	(3)
Loss after tax	**(2)**	(85)
Loss on disposal of businesses including disposal costs	**(8)**	(21)
Loss for the year from discontinued operations	**(10)**	(106)

(1) Operating costs in the year ended 31 December 2019 included a £64 million charge on remeasurement to fair values less costs of disposal relating to the Wheels & Structures business on reclassification to assets held for sale.

14. Property, plant and equipment

	Land and buildings £m	Plant and equipment £m	Total £m
Cost			
At 1 January 2019	943	2,571	3,514
Recognition of right-of-use assets	486	103	589
Additions	89	458	547
Disposals	(25)	(65)	(90)
Transfer to held for sale	(21)	(65)	(86)
Disposal of businesses	(62)	(68)	(130)
Exchange adjustments	(75)	(129)	(204)
At 31 December 2019	1,335	2,805	4,140
Additions	74	230	304
Right-of-use asset reassessments	14	–	14
Acquisition of businesses	3	8	11
Disposals	(33)	(54)	(87)
Exchange adjustments	1	6	7
At 31 December 2020	**1,394**	**2,995**	**4,389**
Accumulated depreciation and impairment			
At 1 January 2019	(62)	(281)	(343)
Charge for the year	(90)	(357)	(447)
Disposals	1	57	58
Transfer to held for sale	3	23	26
Disposal of businesses	1	19	20
Impairments(1)	(27)	(7)	(34)
Exchange adjustments	6	6	12
At 31 December 2019	(168)	(540)	(708)
Charge for the year	(86)	(349)	(435)
Disposals	4	44	48
Impairments(1)	(68)	(93)	(161)
Exchange adjustments	2	(2)	–
At 31 December 2020	**(316)**	**(940)**	**(1,256)**
Net book value			
At 31 December 2020	**1,078**	**2,055**	**3,133**
At 31 December 2019	1,167	2,265	3,432

(1) Includes £141 million (2019: £nil) within impairment of assets and £20 million (2019: £14 million) within restructuring costs both shown as adjusting items (note 6) and £nil (2019: £20 million) of onerous lease liabilities transferred from property related cost provisions.

Property, plant and equipment includes the net book value of right-of-use assets as follows:

Right-of-use asset	Land and buildings £m	Plant and equipment £m	Total £m
At 1 January 2019(1)	57	–	57
IFRS 16 transition adjustment	486	103	589
Additions	59	22	81
Depreciation	(51)	(22)	(73)
Impairments(2)	(28)	(4)	(32)
Disposal of businesses	(28)	(6)	(34)
Transfer to held for sale	–	(2)	(2)
Exchange adjustments	(17)	(3)	(20)
At 31 December 2019	478	88	566
Additions	39	17	56
Depreciation	(52)	(22)	(74)
Impairments	(68)	(14)	(82)
Disposals	(18)	(2)	(20)
Right-of-use asset reassessments	14	–	14
Exchange adjustments	(12)	–	(12)
At 31 December 2020	**381**	**67**	**448**

(1) The balance at 1 January 2019 represented finance lease assets held within property, plant and equipment prior to the adoption of IFRS 16.
(2) Included a £20 million reduction in right-of-use assets following the transfer of onerous lease liabilities from property related cost provisions.

Notes to the Financial Statements
Continued

15. Equity accounted investments

	31 December 2020 £m	31 December 2019 £m
Aggregated amounts relating to equity accounted investments:		
Share of current assets	**334**	278
Share of non-current assets	**371**	386
Share of current liabilities	**(263)**	(205)
Share of non-current liabilities	**(12)**	(23)
Interests in equity accounted investments	**430**	436

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

Group share of equity accounted investments	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
At 1 January	**436**	492
Share of results of equity accounted investments	**32**	38
Dividends paid to the Group	**(54)**	(67)
Disposal of businesses	**–**	(4)
Exchange adjustments	**16**	(23)
At 31 December	**430**	436

Within the Group's share of equity accounted investments there is one significant joint venture, held within the Automotive segment, Shanghai GKN HUAYU Driveline Systems Co Limited ("SDS"). SDS had total sales in the year of £1,101 million (2019: £1,158 million), adjusted operating profit of £116 million (2019: £123 million), adjusting items of £44 million (2019: £39 million), statutory operating profit of £72 million (2019: £84 million), an interest charge of £nil (2019: £nil) and a tax charge of £15 million (2019: £13 million), leaving retained profit of £57 million (2019: £71 million).

Total net assets of SDS at 31 December 2020 were £798 million (31 December 2019: £816 million). These comprised non-current assets of £684 million (31 December 2019: £710 million), current assets of £598 million (31 December 2019: £488 million), current liabilities of £484 million (31 December 2019: £382 million) and non-current liabilities of £nil (31 December 2019: £nil). During 2020, SDS paid a dividend to the Group of £53 million (2019: £65 million). Further information about SDS can be found in note 3 to the Melrose Industries PLC Company Financial Statements.

16. Inventories

	31 December 2020 £m	31 December 2019 £m
Raw materials	**481**	597
Work in progress	**292**	329
Finished goods	**353**	406
	1,126	1,332

In 2020 the write down of inventories to net realisable value amounted to £163 million (2019: £68 million), of which £1 million (2019: £6 million) related to restructuring activities and is included within adjusting items. The reversal of write downs amounted to £65 million (2019: £38 million). Write downs and reversals in both years relate to ongoing assessments of inventory obsolescence, excess inventory holding and inventory resale values across all of the Group's businesses. Included in the amounts above is a charge of £14 million (2019: £nil) relating to the write down of assets in the year, shown as an adjusting item (note 6).

The Directors consider that there is no material difference between the net book value of inventories and their replacement cost.

17. Trade and other receivables

Current	**31 December 2020 £m**	31 December 2019 £m
Trade receivables	**1,269**	1,473
Allowance for expected credit loss	**(41)**	(47)
Other receivables	**258**	298
Prepayments	**54**	71
Contract assets	**118**	175
	1,658	1,970

Trade receivables are non interest-bearing. Credit terms offered to customers vary upon the country of operation but are generally between 30 and 90 days.

Non-current	**31 December 2020 £m**	31 December 2019 £m
Other receivables	**13**	2
Contract assets	**426**	422
	439	424

As described in note 25, certain businesses participate in receivables working capital programmes and have the ability to choose whether to receive payment earlier than the normal due date, for specific customers on a non-recourse basis. As at 31 December 2020, eligible receivables under these programmes have been factored and derecognised in line with the derecognition criteria of IFRS 9.

An allowance has been made for expected lifetime credit losses with reference to past default experience and management's assessment of credit worthiness over trade receivables, an analysis of which is as follows:

	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Management £m	Other Industrial £m	Discontinued Operations £m	Total £m
At 1 January 2019	15	6	3	7	9	2	42
Income Statement charge	1	7	2	–	5	1	16
Utilised	(3)	–	–	–	(2)	–	(5)
Disposal of businesses	–	–	–	–	–	(2)	(2)
Transfer to assets held for sale	–	–	–	–	–	(1)	(1)
Exchange adjustments	(1)	(1)	–	(1)	–	–	(3)
At 31 December 2019	12	12	5	6	12	–	47
Income Statement charge/(credit)	3	–	–	1	(3)	–	1
Utilised	(3)	(1)	–	(1)	(2)	–	(7)
At 31 December 2020	**12**	**11**	**5**	**6**	**7**	**–**	**41**

The concentration of credit risk is limited due to the large number of unrelated customers. Credit control procedures are implemented to ensure that sales are only made to organisations that are willing and able to pay for them. Such procedures include the establishment and review of customer credit limits and terms. The Group does not hold any collateral or any other credit enhancements over any of its trade receivables nor does it have a legal right of offset against any amounts owed by the Group to the counterparty.

17. Trade and other receivables continued

The ageing of impaired trade receivables past due is as follows:

	31 December 2020 £m	31 December 2019 £m
0 – 30 days	15	15
31 – 60 days	1	1
60+ days	25	31
	41	47

Included in the Group's trade receivables balance are overdue trade receivables with a gross carrying amount of £97 million (31 December 2019: £154 million) against which a provision of £41 million (31 December 2019: £47 million) is held.

There are no amounts provided against balances that are not overdue as these are deemed recoverable, following an assessment for impairment in accordance with policies described in note 2.

The ageing of the balance deemed recoverable of £56 million (31 December 2019: £107 million) is as follows:

	31 December 2020 £m	31 December 2019 £m
0 – 30 days	41	72
31 – 60 days	10	24
60+ days	5	11
	56	107

The Directors consider that the carrying amount of trade and other receivables approximates to their fair value.

The Group's contract assets comprise the following:

	Participation fees £m	Unbilled receivables £m	Variable consideration £m	Other £m	Total £m
At 1 January 2019	213	145	206	32	596
Additions	10	1,192	60	25	1,287
Utilised	(12)	(1,227)	(15)	(6)	(1,260)
Exchange adjustments	(9)	(5)	(9)	(3)	(26)
At 31 December 2019	202	105	242	48	597
Additions	9	1,096	26	5	1,136
Utilised	(11)	(1,149)	(13)	(3)	(1,176)
Exchange adjustments	(5)	–	(8)	–	(13)
At 31 December 2020	**195**	**52**	**247**	**50**	**544**

An assessment for impairment of contract assets has been performed in accordance with policies described in note 2. No such impairment has been recorded.

Participation fees
Participation fees are described in the accounting policies (note 2) and are considered to be a reduction in revenue for the related customer contract. Amounts are capitalised and 'amortised' to match to the related performance obligation.

Unbilled receivables for over time recognition
Unbilled receivables for over time recognition represent work completed with associated margins where contracts contain a legal right to compensation for work completed, including a margin, and there is no alternative use for the customer's asset.

Variable consideration
Variable consideration only has a material impact on one entity in the Group, exclusively relating to certain RRSP arrangements in the Aerospace business. RRSP contracting is a feature of the aircraft engine market and typically reflects the engine manufacturer's economic model where discounts are given on the sale of original equipment ("OE") and generally a higher value is associated with the subsequent maintenance, repair and overhaul services. The nature of RRSP arrangements is covered further in the accounting policies (note 2) and the impact on the Group is that OE products sold to engine manufacturers are at a lower margin with more favourable pricing in the aftermarket phase. As a partner in the arrangements, the Aerospace business's cash compensation profile often reflects that of the OE engine manufacturer.

Where the Group has a contractual right to aftermarket revenue, IFRS 15 requires that the total contract revenue is allocated to the performance obligations. The principal contractual term that determines the existence of variable consideration is the absence of a termination clause that the customer can unilaterally exercise and which results in future purchases being considered optional. Where there is such a termination clause and the Group commercially relies on economic compulsion of the contracting parties, the two phases of activity are treated as distinct and no variable consideration is recognised. In the absence of such a term, there is a contractual link between the sale of OE components and aftermarket, which results in variable consideration, and the total contract revenue is allocated to the distinct performance obligations.

17. Trade and other receivables continued

Variable consideration is measured using a weighted average unit method, taking account of an estimate of stand-alone selling price for individual performance obligations and is recognised when control of the OE component passes to the customer (the engine manufacturer). Due to the long-term nature of agreements, calculation of the total programme revenues is inherently imprecise and as set out in note 3e requires significant estimates, including an assessment of the aftermarket revenue per engine which reflects the pattern of future maintenance activity and associated costs to be incurred. In order to address the future uncertainties, risk adjustments as well as constraints have been applied to the expected level of revenue as appropriate. This approach best represents the value of goods and services supplied taking account of the performance obligations, risk and overall contract revenues.

As a consequence of allocating additional revenue to the sale of OE components, a variable consideration contract asset has been recognised which will be satisfied through cash receipt during the aftermarket phase. The constraint applied to variable consideration is reassessed at each period end, and will unwind as risks reduce and when uncertainties are resolved. This is expected to lead to additional revenue recognition in future periods in relation to items sold in the current and preceding periods.

18. Cash and cash equivalents

	31 December 2020 £m	Restated[1] 31 December 2019 £m
Cash and cash equivalents	311	512

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

Cash and cash equivalents comprises cash at bank and in hand which earns interest at floating rates based on daily bank deposit rates and short-term deposits which are made for varying periods of between one day and one month. The carrying amount of these assets is considered to be equal to their fair value.

19. Trade and other payables

Current	31 December 2020 £m	31 December 2019 £m
Trade payables	1,153	1,223
Other payables	417	387
Customer advances and contract liabilities	397	343
Other taxes and social security	91	74
Government refundable advances	7	7
Accruals	371	413
Deferred government grants	20	14
	2,456	2,461

As at 31 December 2020, and as described in note 25, included within trade payables were drawings on supplier finance facilities of £62 million (31 December 2019: £75 million).

Trade payables are non-interest-bearing. Normal settlement terms vary by country and the average credit period taken for trade and other payables is 69 days (31 December 2019: 78 days).

Non-current	31 December 2020 £m	31 December 2019 £m
Other payables	13	11
Customer advances and contract liabilities	304	352
Other taxes and social security	3	2
Government refundable advances	51	59
Accruals	36	2
Deferred government grants	14	18
	421	444

The Directors consider that the carrying amount of trade and other payables approximates to their fair value.

Non-current amounts owed to suppliers fall due within two years. Government refundable advances are forecast to fall due for repayment between 2021 and 2055.

Customer advances and contract liabilities include cash receipts from customers in advance of the Group completing its performance obligations and is generally utilised as product is delivered. Non-current amounts in respect of customer advances and contract liabilities will be utilised as follows: one to two years £90 million, two to five years £124 million and over five years £90 million (31 December 2019: one to two years £132 million, two to five years £154 million and over five years £66 million).

20. Interest-bearing loans and borrowings

This note provides information about the contractual terms of the Group's interest-bearing loans and borrowings. Details of the Group's exposure to credit, liquidity, interest rate and foreign currency risk are included in note 25.

	Current		Non-current		Total	
	31 December 2020 £m	Restated[1] 31 December 2019 £m	**31 December 2020 £m**	31 December 2019 £m	**31 December 2020 £m**	Restated[1] 31 December 2019 £m
Floating rate obligations						
Bank borrowings – US Dollar loan	**–**	–	**1,850**	2,199	**1,850**	2,199
Bank borrowings – Sterling loan	**–**	–	**254**	520	**254**	520
Other loans and bank overdrafts	**151**	195	**80**	–	**231**	195
Fixed rate obligations						
2022 £450 million bond	**–**	–	**450**	450	**450**	450
2032 £300 million bond	**–**	–	**300**	300	**300**	300
Other loans	**3**	78	**–**	3	**3**	81
	154	273	**2,934**	3,472	**3,088**	3,745
Unamortised finance costs[2]	**–**	–	**(19)**	(30)	**(19)**	(30)
Non-cash acquisition fair value adjustment	**11**	11	**11**	22	**22**	33
Total interest-bearing loans and borrowings	**165**	284	**2,926**	3,464	**3,091**	3,748

(1) Current interest-bearing loans and borrowings has been restated to meet the requirements of IAS 32 as further described in note 1. This has had no impact on net assets.
(2) Includes £1 million of debt issue costs paid during the year (2019: £nil).

The Group's committed bank funding includes: a multi-currency denominated term loan of £100 million and US$960 million that was due to mature in April 2021; and a multi-currency denominated revolving credit facility of £1.1 billion, US$2.0 billion and €0.5 billion that matures in January 2023. In February 2021, the Group exercised its option to extend the term loan for a further three years to April 2024. Loans drawn under this facility are guaranteed by Melrose Industries PLC and certain of its subsidiaries, and there is no security over any of the Group's assets in respect of this facility.

At 31 December 2020 the term loan was fully drawn and there was a significant amount of headroom on the multi-currency revolving credit facility. Applying the exchange rates at 31 December 2020 the headroom equated to £1,632 million. There are also a number of uncommitted overdraft, guarantee and borrowing facilities made available to the Group.

Throughout the year, the Group remained compliant with all covenants under the facilities disclosed above. A number of Group companies continue to be guarantors under the bank facilities. Further details on covenant compliance for the year ended 31 December 2020 are contained in note 25.

Drawdowns under the existing facilities bear interest at interbank rates plus a margin determined by reference to the Group's performance under its debt cover ratio, ranging between 0.75% to 2.0% on the term loan, and 0.95% to 2.25% on the revolving credit facility. As at 31 December 2020 the margin was 2.0% (31 December 2019: 1.4%) on the term loan and 2.25% (31 December 2019: 1.65%) on the revolving credit facility.

The £450 million bond maturing in 2022 has associated cross-currency swaps. Details of the bonds are in the table below:

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

The coupon rate on the £300 million bond, maturing in 2032, increased from 3.375% to 4.625% in May 2019.

Maturity of financial liabilities (excluding currency contracts and lease obligations)

The table below shows the maturity profile of anticipated future cash flows, including interest, on an undiscounted basis in relation to the Group's financial liabilities (other than those associated with currency risk, which are shown in note 25, and lease obligations which are shown in note 28). The amounts shown therefore differ from the carrying value and fair value of the Group's financial liabilities.

	Interest-bearing loans and borrowings £m	Interest rate derivative financial liabilities £m	Other financial liabilities £m	Total financial liabilities £m
Within one year	242	33	1,948	2,223
In one to two years	539	34	53	626
In two to five years	2,252	22	17	2,291
After five years	397	–	30	427
Effect of financing rates	(339)	(2)	–	(341)
31 December 2020	**3,091**	**87**	**2,048**	**5,226**
Within one year	393	11	2,030	2,434
In one to two years	929	14	33	976
In two to five years	2,495	35	21	2,551
After five years	411	–	18	429
Effect of financing rates	(480)	–	–	(480)
31 December 2019 (restated)[1]	3,748	60	2,102	5,910

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

21. Provisions

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

(1) Includes £234 million of adjusting items and £204 million recognised in adjusted operating profit.
(2) Includes £147 million of adjusting items and £35 million recognised in adjusted operating profit.
(3) Includes £2 million within finance costs relating to the time value of money and £4 million relating to changes in discount rates on loss-making contract provisions recognised as fair value items on the acquisition of GKN, which has been included as an adjusting item within operating profit (note 6).

Loss-making contracts

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

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

Utilisation during the year of £59 million (2019: £83 million) has benefited adjusted operating profit with £32 million recognised in Aerospace, £21 million recognised in Automotive, £5 million recognised in Powder Metallurgy and £1 million recognised in Other Industrial. In addition, £93 million has been released on a net basis with a net £101 million shown as an adjusting item, as described in note 6, as part of the release of fair value items split; £72 million in Aerospace, £36 million in Powder Metallurgy and a charge of £7 million in Automotive.

Property related costs

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

Environmental and litigation

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

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

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

Warranty related costs

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

Restructuring

Restructuring provisions relate to committed costs in respect of restructuring programmes, as described in note 6, usually resulting in cash spend within one year. A restructuring provision is recognised when the Group has developed a detailed formal plan for the restructuring and has raised a valid expectation in those affected that it will carry out the restructuring by either starting to implement the plan or by announcing its main features to those affected by it. The measurement of a restructuring provision includes only the direct expenditures arising from the restructuring, which are those amounts that are necessarily entailed by the restructuring programmes.

Other

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

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

22. Deferred tax

The following are the major deferred tax assets and liabilities recognised by the Group and movements thereon during the current and prior reporting period.

	Deferred tax assets	Deferred tax liabilities			
	Tax losses and other assets £m	Accelerated capital allowances and other liabilities £m	Deferred tax on intangible assets £m	Total deferred tax liabilities £m	Total net deferred tax £m
At 1 January 2019	132	(166)	(708)	(874)	(742)
Transfer to held for sale	(6)	2	–	2	(4)
Disposal of businesses	(25)	1	33	34	9
(Charge)/credit to income	(13)	(15)	124	109	96
Charge to equity	(4)	–	–	–	(4)
Exchange adjustments	(19)	1	51	52	33
Movement in set off of assets and liabilities(1)	95	3	(98)	(95)	–
At 31 December 2019	160	(174)	(598)	(772)	(612)
Acquisition of businesses	–	–	(5)	(5)	(5)
Credit/(charge) to income	17	(13)	84	71	88
Charge to equity	(33)	–	–	–	(33)
Exchange adjustments	7	1	2	3	10
Movement in set off of assets and liabilities(1)	29	19	(48)	(29)	–
At 31 December 2020	**180**	**(167)**	**(565)**	**(732)**	**(552)**

(1) Set off of deferred tax assets and liabilities in accordance with IAS 12 within territories with a right of set off.

As at 31 December 2020, the Group had gross unused corporate income tax losses of £2,166 million (31 December 2019: £2,036 million) available for offset against future profits. A deferred tax asset of £290 million (31 December 2019: £204 million) has been recognised in respect of £1,337 million (31 December 2019: £1,052 million) of these gross losses. No asset has been recognised in respect of the remaining losses due to the divisional and geographic split of anticipated future profit streams. Most of these losses may be carried forward indefinitely subject to certain continuity of business requirements. Where losses are subject to time expiry, a deferred tax asset is recognised to the extent that sufficient future profits are anticipated to utilise these losses. In addition to the corporate income tax losses included above, a deferred tax asset of £60 million (31 December 2019: £46 million) has been recognised on tax credits (primarily US) and US state tax losses.

Deferred tax assets have also been recognised on Group retirement benefit obligations at £122 million (31 December 2019: £122 million) and on other temporary differences at £338 million (31 December 2019: £447 million). The gross deferred tax assets therefore amount to £810 million (31 December 2019: £819 million).

Deferred tax liabilities have been recognised on intangible assets at £1,161 million (31 December 2019: £1,243 million) and accelerated capital allowances and other temporary differences at £201 million (31 December 2019: £188 million). The gross deferred tax liabilities therefore amount to £1,362 million (31 December 2019: £1,431 million).

There are no material unrecognised deferred tax assets at 31 December 2020, other than the losses referred to above.

No deferred tax is recognised on the unremitted earnings of overseas subsidiaries except where the distribution of such profits is planned. If these earnings were remitted in full, tax of £65 million (31 December 2019: £51 million) would be payable. Following the UK's exit from the EU, the Group will rely on withholding tax rates as set out in Double Taxation Conventions agreed between the UK and other countries. The unrecognised deferred tax is higher as a result, primarily on dividend receipts from Germany and Italy.

23. Share-based payments

2017 Incentive Plan and 2020 Employee Share Plan

The 2017 Incentive Plan was approved on 11 May 2017 and comprised 50,000 2017 options which enabled the holders to subscribe for 2017 Incentive Shares. These options were issued to Directors and Senior Management in three annual tranches. For accounting purposes, the IFRS 2 charge was calculated as if all three tranches had been granted on day one because of a common expectation, established at that date, between employees and the Company that the options would be allocated annually over the three year performance period. The 2017 Incentive Plan crystallised on 31 May 2020 and the value of the scheme on crystallisation was £nil. Accordingly, no Ordinary Shares were issued to the participants of the 2017 Incentive Plan.

The 2020 Employee Share Plan was approved on 21 January 2021. An IFRS 2 charge has however been recognised from 1 June 2020, the start date of the 2020 Employee Share Plan, because employees rendered services to the Company from that date and there was a common expectation between the employees and the Company that the 2020 Employee Share Plan would be agreed.

Further details of the crystallisation of the 2017 Incentive Plan and the 2020 Employee Share Plan are set out in the Directors' Remuneration Report on pages 116 and 117.

During the year, the Group recognised a charge of £1 million (2019: £17 million) in respect of the 2017 Incentive Plan, inclusive of a £4 million credit in respect of related national insurance (2019: charge of £4 million) and a charge of £10 million (2019: £nil) in respect of the 2020 Employee Share Plan, inclusive of a £1 million charge in respect of related national insurance (2019: £nil).

The estimated value of the 2020 Employee Share Plan at 31 December 2020 if settled at that date was £33 million (31 December 2019: value of the 2017 Incentive Plan was £nil). Using a Black-Scholes option pricing model, the projected value of this plan at 31 May 2023 (being the end of the three year performance period) will be £34 million (31 December 2019: projected value of the 2017 Incentive Plan at 31 May 2020 was £39 million). The projected value is impacted by future acquisition and disposal assumptions.

23. Share-based payments continued

The annual IFRS 2 charge to be recognised in respect of the 2020 Employee Share Plan is £16 million. The inputs into the Black-Scholes valuation model that were used to fair value the plan at the grant date were as follows:

	Valuation assumptions
Weighted average share price	**£1.81**
Weighted average exercise price	**£1.71**
Expected volatility	**58%**
Expected life as at inception	**2.4 years**
Risk free interest	**0.0%**

Expected volatility was determined by calculating the historical volatility of the Company's share price.

24. Retirement benefit obligations

Defined contribution plans

The Group operates defined contribution plans for qualifying employees across several jurisdictions. The assets of the plans are held separately from those of the Group in funds under the control of trustees.

The total costs charged in relation to the continuing businesses during the year of £69 million (2019: £86 million) represent contributions payable to these plans by the Group at rates specified in the rules of the plans.

Defined benefit plans

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

The most significant defined benefit pension plans in the Group at 31 December 2020 were:

GKN Group Pension Schemes (Numbers 1 – 4)

The GKN Group Pension Schemes (Numbers 1 – 4), which are shown within the Aerospace and Automotive segments, net liabilities are split 58% and 42% respectively as at 31 December 2020, are funded plans, closed to new members and were closed to future accrual in 2017. The valuation of the plans was based on a full actuarial valuation as of 30 June 2019, updated to 31 December 2020 by independent actuaries.

GKN UK 2016 Pension Plan

The GKN UK 2016 Pension Plan is a funded plan, closed to new members with no active members, containing assets and liabilities in respect of the pension schemes from various legacy GKN businesses. The valuation of the plan was based on a full actuarial valuation as of 5 April 2019, updated to 31 December 2020 by independent actuaries.

GKN US Consolidated Pension Plan

The GKN US Consolidated Pension Plan is a funded plan, closed to new members and closed to future accrual. The US Pension Plan valuation was based on a full actuarial valuation as of 1 January 2020, updated to 31 December 2020 by independent actuaries.

GKN Germany Pension Plans

The GKN Germany Pension Plans provide benefits dependent on final salary and service with the Company. The plans are generally unfunded and closed to new members.

Brush UK Pension Plan

The Brush Group (2013) ("Brush UK") Pension Plan is a funded plan, closed to new members and closed to future accrual. The valuation of the Brush UK Pension Plan was based on a full actuarial valuation as of 31 December 2019, updated to 31 December 2020 by independent actuaries.

Other plans include a number of funded and unfunded defined benefit arrangements and retiree medical insurance plans, predominantly in the US and Europe.

The cost of the Group's defined benefit plans is determined in accordance with IAS 19 (revised): "Employee benefits" using the advice of independent professionally qualified actuaries on the basis of formal actuarial valuations and using the projected unit credit method. In line with normal practice, these valuations are undertaken triennially in the UK and annually in the US and Germany.

Contributions

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

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

24. Retirement benefit obligations continued

Actuarial assumptions

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

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

Mortality

GKN Group Pension Schemes (Numbers 1 – 4), GKN UK 2016 Pension Plan and the Brush UK Pension Plan

Mortality assumptions for the Brush UK Pension Plan as at 31 December 2020 were based on the Self Administered Pension Scheme ("SAPS") "S3" base tables, using a scaling factor of 112%. The GKN Group Pension Schemes (Numbers 1 – 4) and the GKN UK 2016 Pension Plan use the SAPS "S3PA" base tables with scheme-specific adjustments. The base table mortality assumption for each of the UK plans reflects best estimate results from the most recent mortality experience analyses for each scheme. Weighting factors vary by scheme.

Future improvements for all UK plans are in line with the 2019 Continuous Mortality Investigation ("CMI") core projection model (SK = 7.0, A = 0%) with a long-term rate of improvement of 1.25% p.a. for both males and females.

GKN US Consolidated Pension Plan

GKN US Pension and Medical Plans use base mortality tables that are adjusted for recent plan experience (equivalent to RP2006 projected to 2018 using scale MP2018 with a 6.1001% load). Future improvements for all US plans are in line with MP2020.

GKN Germany Pension Plans

All German plans use the Richttafein 2018 G tables, with no adjustment.

The following table shows the future life expectancy of individuals age 65 at the year end and the future life expectancy of individuals aged 65 in 20 years' time.

	GKN Group Pension Schemes (Numbers 1 – 4) years	GKN UK 2016 Pension Plan years	GKN US Consolidated Pension Plan years	GKN Germany Pension Plans years	Brush UK Pension Plan years
Male today	21.3	21.4	19.0	20.3	21.1
Female today	24.2	23.8	21.0	23.8	23.5
Male in 20 years' time	22.3	22.7	20.5	23.1	22.4
Female in 20 years' time	25.7	25.3	22.4	26.0	24.9

Balance Sheet disclosures

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

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

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

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

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

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

24. Retirement benefit obligations continued

The major categories and fair values of plan assets at the end of the reporting period for each category were as follows:

	31 December 2020 £m	31 December 2019 £m
Equities	**699**	749
Government bonds	**1,164**	1,051
Corporate bonds	**671**	437
Property	**96**	97
Insurance contracts	**162**	174
Multi-strategy/Diversified growth funds	**83**	432
Private equity	**175**	177
Other(1)	**725**	295
Total	**3,775**	3,412

(1) Primarily consists of cash collateral and liability driven investments.

The assets were well diversified and the majority of plan assets had quoted prices in active markets. All government bonds were issued by reputable governments and were generally AA rated or higher. Interest rate and inflation rate swaps were also employed to complement the role of fixed and index-linked bond holdings for liability risk management.

The trustees continually review whether the chosen investment strategy is appropriate with a view to providing the pension benefits and to ensure appropriate matching of risk and return profiles. The main strategic policies included maintaining an appropriate asset mix, managing interest rate sensitivity and maintaining an appropriate equity buffer. Investment results are regularly reviewed.

Movements in the present value of defined benefit obligations during the year:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
At 1 January	**4,533**	4,686
Current service cost	**10**	12
Past service cost/(credit)(1)	**2**	(4)
Interest cost on obligations	**88**	125
Remeasurement losses/(gains) – demographic	**7**	(157)
Remeasurement losses – financial	**365**	569
Remeasurement gains – experience	**(178)**	(1)
Benefits paid out of plan assets	**(192)**	(181)
Benefits paid out of Group assets for unfunded plans	**(36)**	(28)
Settlements	**(7)**	(261)
Disposal of businesses	**–**	(175)
Exchange adjustments	**21**	(52)
At 31 December	**4,613**	4,533

(1) An expense of £2 million was recorded in the year ended 31 December 2020 as a past service cost in respect of the equalisation of guaranteed minimum pension ("GMP") benefits in the UK. This was treated as an adjusting item (note 6). A credit of £4 million was recorded in the year ended 31 December 2019 as a past service cost following a curtailment gain on a GKN Germany pension scheme. This was treated as an adjusting item in restructuring (note 6).

The defined benefit plan liabilities were 20% (31 December 2019: 27%) in respect of active plan participants, 27% (31 December 2019: 26%) in respect of deferred plan participants and 53% (31 December 2019: 47%) in respect of pensioners.

The weighted average duration of the defined benefit plan liabilities at 31 December 2020 was 16.4 years (31 December 2019: 17.1 years).

Movements in the fair value of plan assets during the year:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
At 1 January	**3,412**	3,273
Interest income on plan assets	**69**	93
Return on plan assets, excluding interest income	**438**	379
Contributions	**75**	157
Benefits paid out of plan assets	**(192)**	(181)
Plan administrative costs	**(14)**	(15)
Settlements	**(7)**	(262)
Disposal of businesses	**–**	(20)
Exchange adjustments	**(6)**	(12)
At 31 December	**3,775**	3,412

The actual return on plan assets was a gain of £507 million (2019: £472 million).

Notes to the Financial Statements
Continued

24. Retirement benefit obligations continued
Income Statement disclosures
Amounts recognised in the Consolidated Income Statement in respect of these defined benefit plans were as follows:

Continuing operations	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Included within operating (loss)/profit:		
– current service cost	**10**	12
– past service cost/(credit)(1)	**2**	(4)
– plan administrative costs	**14**	15
Included within net finance costs:		
– interest cost on defined benefit obligations	**88**	124
– interest income on plan assets	**(69)**	(93)

Discontinued operations	**Year ended 31 December 2020 £m**	Year ended 31 December 2019 £m
Included within net finance costs:		
– interest cost on defined benefit obligations	**–**	1

(1) An expense of £2 million was recorded in the year ended 31 December 2020 as a past service cost in respect of the equalisation of guaranteed minimum pension ("GMP") benefits in the UK. This was treated as an adjusting item (note 6). A credit of £4 million was recorded in the year ended 31 December 2019 as a past service cost following a curtailment gain on a GKN Germany pension scheme. This was treated as an adjusting item in restructuring (note 6).

Statement of Comprehensive Income disclosures
Amounts recognised in the Consolidated Statement of Comprehensive Income in respect of these defined benefit plans were as follows:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Return on plan assets, excluding interest income	**438**	379
Remeasurement (losses)/gains arising from changes in demographic assumptions	**(7)**	157
Remeasurement losses arising from changes in financial assumptions	**(365)**	(569)
Remeasurement gains arising from experience adjustments	**178**	1
Net remeasurement gain/(loss) on retirement benefit obligations	**244**	(32)

Risks and sensitivities
The defined benefit plans expose the Group to actuarial risks, such as longevity risk, inflation risk, interest rate risk and market (investment) risk. The Group is not exposed to any unusual, entity specific or plan specific risks.

A sensitivity analysis on the principal assumptions used to measure the plan liabilities at the year end was as follows:

	Change in assumption	Decrease/(increase) to plan liabilities £m	Increase/(decrease) to profit before tax £m
Discount rate	Increase by 0.1 ppts	74	1
	Decrease by 0.1 ppts	(78)	(1)
Inflation assumption(1)	Increase by 0.1 ppts	(46)	n/a
	Decrease by 0.1 ppts	48	n/a
Assumed life expectancy at age 65 (rate of mortality)	Increase by 1 year	(250)	n/a
	Decrease by 1 year	249	n/a

(1) The inflation sensitivity encompasses the impact on pension increases, where applicable.

The sensitivity analysis above was determined based on reasonably possible changes to the respective assumptions, while holding all other assumptions constant. There has been no change in the methods and assumptions used in preparing the sensitivity analysis from prior years.

The sensitivities are based on the relevant assumptions and membership profile as at 31 December 2020 and are applied to the obligations at the end of the reporting period. Whilst the analysis does not take account of the full distribution of cash flows expected, it does provide an approximation to the sensitivity of the assumptions shown. Extrapolation of these results beyond the sensitivity figures shown may not be appropriate and the sensitivity analysis presented may not be representative of the actual change in the defined benefit obligation as it is unlikely that the change in assumptions would occur in isolation of one another as some of the assumptions may be correlated.

25. Financial instruments and risk management
The table below sets out the Group's accounting classification of each category of financial assets and liabilities and their carrying values at 31 December 2020 and 31 December 2019:

	Aerospace £m	Automotive £m	Powder Metallurgy £m	Nortek Air Management £m	Other Industrial £m	Corporate £m	Discontinued Operations £m	**Total £m**
31 December 2020								
Financial assets								
Classified as amortised cost:								
Cash and cash equivalents	–	–	–	–	–	311	–	**311**
Net trade receivables	453	372	143	173	87	–	–	**1,228**
Classified as fair value:								
Investments	34	–	–	–	–	–	–	**34**
Derivative financial assets								
Foreign currency forward contracts	–	1	–	5	3	126	–	**135**
Embedded derivatives(1)	13	–	–	–	–	–	–	**13**
Financial liabilities								
Classified as amortised cost:								
Interest-bearing loans and borrowings	–	–	–	–	–	(3,091)	–	**(3,091)**
Government refundable advances	(58)	–	–	–	–	–	–	**(58)**
Lease obligations	(266)	(113)	(59)	(90)	(24)	(3)	–	**(555)**
Other financial liabilities	(564)	(899)	(179)	(195)	(100)	(53)	–	**(1,990)**
Classified as fair value:								
Derivative financial liabilities								
Foreign currency forward contracts	–	(4)	–	(13)	–	(69)	–	**(86)**
Interest rate swaps	–	–	–	–	–	(87)	–	**(87)**
Cross-currency swaps	–	–	–	–	–	(89)	–	**(89)**
Embedded derivatives(1)	(6)	–	–	–	–	–	–	**(6)**
31 December 2019 (restated)								
Financial assets								
Classified as amortised cost:								
Cash and cash equivalents(2)	–	–	–	–	–	512	–	512
Net trade receivables	626	402	155	141	102	–	–	1,426
Classified as fair value:								
Investments	48	–	–	–	–	–	–	48
Derivative financial assets								
Foreign currency forward contracts	–	–	–	2	1	37	–	40
Interest rate swaps	–	–	–	–	–	1	–	1
Embedded derivatives(1)	16	–	–	–	–	–	–	16
Assets classified as held for sale	–	–	–	–	–	–	65	65
Financial liabilities								
Classified as amortised cost:								
Interest-bearing loans and borrowings(2)	–	–	–	–	–	(3,748)	–	(3,748)
Government refundable advances	(66)	–	–	–	–	–	–	(66)
Lease obligations	(287)	(117)	(59)	(89)	(26)	(4)	–	(582)
Other financial liabilities	(741)	(842)	(138)	(154)	(115)	(46)	–	(2,036)
Classified as fair value:								
Derivative financial liabilities								
Foreign currency forward contracts	–	(2)	–	(1)	(1)	(170)	–	(174)
Interest rate swaps	–	–	–	–	–	(60)	–	(60)
Cross-currency swaps	–	–	–	–	–	(80)	–	(80)
Embedded derivatives(1)	(8)	–	–	–	–	–	–	(8)
Liabilities associated with assets held for sale	–	–	–	–	–	–	(46)	(46)

(1) The embedded derivative is classified as a level 3 fair value under the IFRS 13 fair value hierarchy.
(2) As disclosed in note 1, the Group's cash pooling arrangements have been restated to meet the presentational requirements for offsetting in accordance with IAS 32.

Reconciliation of liabilities arising from financing activities
Liabilities arising from financing activities, as defined by IAS 7, totalled £4,215 million at 31 December 2019 comprising; external debt of £3,553 million (excluding £195 million of bank overdrafts), cross-currency swaps of £80 million and lease obligations of £582 million. During the year a cash outflow in those liabilities totalled £674 million as follows: repayment of external debt and cross-currency swaps associated with debt of £598 million (note 27) and repayment of principal on lease obligations of £76 million (note 28). Whilst there is a payment of £1 million included within the financing activities section of the Consolidated Statement of Cash Flows, in respect of costs of raising debt finance, this does not affect liabilities arising from financing activities. There is also an increase to liabilities arising from financing activities relating to non-cash items totalling £43 million comprising; a reduction in external debt and cross-currency swaps associated with debt of £6 million due to changes in foreign exchange rates and an increase in respect of lease obligations of £49 million. As at 31 December 2020, liabilities arising from financing activities, as defined by IAS 7, totalled £3,584 million comprising; external debt of £2,940 million (excluding £151 million of bank overdrafts), cross-currency swaps of £89 million and lease obligations of £555 million.

25. Financial instruments and risk management continued

Liabilities arising from financing activities, as defined by IAS 7, totalled £4,011 million at 31 December 2018 comprising; external debt of £3,755 million (excluding £96 million of bank overdrafts), cross-currency swaps of £199 million and lease obligations of £57 million. During the year a cash outflow in those liabilities totalled £276 million as follows: repayment of external debt and cross-currency swaps associated with debt of £206 million (note 27) of which £100 million is recorded as an investing activity in the Consolidated Statement of Cash Flows and repayment of principal on lease obligations of £70 million. Payments of £237 million included within the financing activities section of the Consolidated Statement of Cash Flows, in respect of dividends paid to non-controlling interests and to owners of the parent, do not affect liabilities arising from financing activities. There is also an increase to liabilities arising from financing activities relating to non-cash items totalling £480 million comprising; a reduction in external debt and cross-currency swaps associated with debt of £115 million due to changes in foreign exchange rates and other non-cash movements and an increase in respect of lease obligations of £595 million. As at 31 December 2019, liabilities arising from financing activities, as defined by IAS 7, totalled £4,215 million comprising; external debt of £3,553 million (excluding £195 million of bank overdrafts), cross-currency swaps of £80 million and lease obligations of £582 million.

Fair values

As at 31 December 2020, the £450 million bond maturing in 2022 had a carrying value of £467 million (31 December 2019: £478 million) and a fair value of £478 million (31 December 2019: £490 million), and the £300 million bond maturing in 2032 had a carrying value of £305 million (31 December 2019: £305 million) and a fair value of £322 million (31 December 2019: £311 million).

The Directors consider that the other financial assets and liabilities have fair values not materially different to the carrying values.

Credit risk

The Group's principal financial assets were cash and cash equivalents, trade receivables and derivative financial assets which represented the Group's maximum exposure to credit risk in relation to financial assets.

The Group's credit risk on cash and cash equivalents and derivative financial assets was limited because the counterparties were banks with strong credit ratings assigned by international credit rating agencies. Exposure is managed on the basis of risk rating and counterparty limits. The value of credit risk in derivative assets has been modelled using publicly available inputs as part of their fair value.

The Group's credit risk was therefore primarily attributable to its trade receivables. The amounts presented in the Consolidated Balance Sheet were net of allowance for expected credit loss, estimated by the Group's management based on prior experience and their assessment of the current economic environment. Note 17 provides further details regarding the recovery of trade receivables.

The following financial assets and liabilities are subject to offsetting, enforceable master netting arrangements and similar agreements:

31 December 2020	Gross amounts of recognised financial assets/(liabilities) £m	Gross amounts of recognised financial assets/(liabilities) set off in the Balance Sheet £m	Net amounts of financial assets/(liabilities) presented in the Balance Sheet £m	Related amounts of financial instruments not set off in the Balance Sheet £m	**Net amount £m**
Cash and cash equivalents	338	(27)	311	(146)	**165**
Derivative financial assets	148	–	148	(131)	**17**
Financial assets subject to master netting arrangements	**486**	**(27)**	**459**	**(277)**	**182**
Interest-bearing loans and borrowings	(3,118)	27	(3,091)	19	**(3,072)**
Derivative financial liabilities	(268)	–	(268)	258	**(10)**
Financial liabilities subject to master netting arrangements	**(3,386)**	**27**	**(3,359)**	**277**	**(3,082)**

31 December 2019	Gross amounts of recognised financial assets/(liabilities) £m	Gross amounts of recognised financial assets/(liabilities) set off in the Balance Sheet £m	Net amounts of financial assets/(liabilities) presented in the Balance Sheet £m	Related amounts of financial instruments not set off in the Balance Sheet £m	Net amount £m
Cash and cash equivalents	512	–	512	(244)	268
Derivative financial assets	57	–	57	(39)	18
Financial assets subject to master netting arrangements	569	–	569	(283)	286
Interest-bearing loans and borrowings	(3,748)	–	(3,748)	–	(3,748)
Derivative financial liabilities	(322)	–	(322)	283	(39)
Financial liabilities subject to master netting arrangements	(4,070)	–	(4,070)	283	(3,787)

Capital risk

The Group manages its capital to ensure that entities in the Group will be able to continue as a going concern.

The capital structure of the Group as at 31 December 2020 consists of net debt, as disclosed in note 27, and equity attributable to the owners of the parent, comprising issued share capital, reserves and retained earnings as disclosed in the Consolidated Statement of Changes in Equity.

25. Financial instruments and risk management continued

Liquidity risk management

Overview of banking facilities

The Group's committed bank funding includes: a multi-currency denominated term loan of £100 million and US$960 million that was due to mature in April 2021; and a multi-currency denominated revolving credit facility of £1.1 billion, US$2.0 billion and €0.5 billion that matures in January 2023. In February 2021, the Group exercised its option to extend the term loan for a further three years to April 2024. Loans drawn under this facility are guaranteed by Melrose Industries PLC and certain of its subsidiaries, and there is no security over any of the Group's assets in respect of this facility.

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

Cash, deposits and marketable securities amounted to £311 million at 31 December 2020 (31 December 2019 (restated): £512 million) and are offset to arrive at the Group net debt position of £2,847 million (31 December 2019: £3,283 million). Cash and cash equivalents and current interest-bearing loans and borrowings have been restated to meet the requirements of IAS 32 as further described in note 1. This has had no impact on net assets. The combination of this cash and the headroom on the revolving credit facility allows the Directors to consider that the Group has sufficient access to liquidity for its current needs. The Board takes careful consideration of counterparty risk with banks when deciding where to place cash on deposit.

Covenants

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

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

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

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

Bonds

Capital market borrowings as at 31 December 2020, inherited as part of the GKN acquisition, consist of a £450 million bond maturing September 2022 and a £300 million bond maturing May 2032. Details of the bonds outstanding at 31 December 2020 are shown in note 20.

The £450 million bond was fully swapped into US$373 million and €284 million by GKN in September 2014 by using a number of cross-currency swaps. At 31 December 2020, the fair value liability of these cross-currency swaps was £80 million (31 December 2019: £74 million).

In respect of the cross-currency swaps on the £450 million bond, during the year there was a charge of £1 million (2019: £1 million) recognised within the cost of hedge reserve related to the cost of hedging. At 31 December 2020, the cumulative value of the cost of hedging recognised within the cost of hedge reserve is £8 million (2019: £7 million).

Working capital

The Group has a small number of uncommitted working capital programmes, which predominantly relate to the programmes inherited as part of the GKN acquisition. These programmes provide favourable financing terms on eligible customer receipts and competitive financing terms to suppliers on eligible supplier payments.

GKN businesses which participate in these customer related finance programmes have the ability to choose whether to receive payment earlier than the normal due date, for specific customers on a non-recourse basis. As at 31 December 2020, the drawings on these facilities were £314 million (31 December 2019: £200 million), and the net cash benefit in the year was approximately £60 million.

In addition, some suppliers have access to utilise the Group's supplier finance programmes, which are provided by a small number of the Group's banks. There is no cost to the Group for providing these programmes to its suppliers. These arrangements do not change the date suppliers are due to be paid by the Group, and therefore there is no additional impact on the Group's liquidity. If the Group exited these arrangements there could be a potential impact of up to £32 million (31 December 2019: £37 million) on the Group's cash flow. These programmes allow suppliers to choose whether they want to accelerate the payment of their invoices, by the financing banks, for an interest cost which is competitive, based on the credit rating of the Group as determined by the financing banks. The amounts owed to the banks are presented in trade payables on the Balance Sheet and the cash flows are presented in cash flows from operating activities. As at 31 December 2020, total facilities were £250 million (31 December 2019: £161 million) with drawings of £62 million (31 December 2019: £75 million). The arrangements do not change the timing of the Group's cash outflows.

25. Financial instruments and risk management continued

Hedge of net investments in foreign entities using loans and derivatives

Interest-bearing loans and borrowings together with cross-currency swaps are designated as hedges of net investments in the Group's subsidiaries in the USA and Europe to reduce the exposure to the related foreign exchange risks.

The value of these were as follows:

	31 December 2020 £m	31 December 2019 £m
Local borrowing:		
US Dollar	**1,478**	1,731
Euro	**381**	473
GKN cross-currency swaps:		
US Dollar	**273**	281
Euro	**255**	241

The foreign exchange movement on the local borrowings, which is recorded in currency translation on net investments within Other Comprehensive Income, was a gain of £61 million (2019: £83 million).

The Euro borrowings include US Dollar debt that was swapped into Euros using cross-currency swaps. The fair value of these cross-currency swaps was a liability of £9 million (31 December 2019: £6 million). The foreign exchange movement on these cross-currency swaps, which is recorded in derivative losses on hedge relationships within Other Comprehensive Income, was a loss of £49 million (2019: £6 million). Net cash settlements in the year totalled £46 million (2019: £nil).

The foreign exchange movement on the GKN cross-currency swaps, which is recorded in derivative losses on hedge relationships, was a loss of £6 million (2019: gain of £25 million).

Finance cost risk management

Drawdowns under the existing facilities bear interest at interbank rates plus a margin determined by reference to the Group's performance under its debt cover ratio, ranging between 0.75% to 2.0% on the term loan, and 0.95% to 2.25% on the revolving credit facility. As at 31 December 2020 the margin was 2.0% (31 December 2019: 1.4%) on the term loan and 2.25% (31 December 2019: 1.65%) on the revolving credit facility.

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

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

The interest rate swaps are designated as cash flow hedges and were highly effective throughout 2020. The fair value of the contracts as at 31 December 2020 was a net liability of £87 million (31 December 2019: £59 million). The net charge of £28 million for the year ended 31 December 2020 (2019: £36 million) being the movement in the year, excluding accrued interest, was booked to derivative losses on hedge relationships within Other Comprehensive Income.

Due to some of the critical terms of the interest rate swaps and the hedged items not being perfectly matched, this could give rise to ineffectiveness through the Income Statement in future periods. This is not expected to be material and no ineffectiveness was booked through the Income Statement in the year ended 31 December 2020 (2019: £nil).

Interest rate sensitivity analysis

Assuming the net debt, inclusive of interest rate swaps, held as at the balance sheet date was outstanding for the whole year, a one percentage point rise in market interest rates for all currencies would decrease profit before tax by the following amounts:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Sterling	**(1)**	(4)
US Dollar	**(2)**	(3)
Euro	**–**	(1)

On the basis of the floating-to-fixed interest rate swaps in place at the balance sheet date, a one percentage point fall in market interest rates for all currencies would decrease Group equity by £35 million (31 December 2019: £51 million).

Exchange rate risk management

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

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

25. Financial instruments and risk management continued

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

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

As at 31 December 2020, the Group held foreign exchange forward contracts to mitigate expected exchange rate fluctuations on future cash flows from sales to customers and purchases from suppliers. The fair value of all foreign exchange forward contracts across the Group was a net asset at 31 December 2020 of £49 million (31 December 2019: net liability of £134 million). A small proportion of these contracts have been designated as cash flow hedges within the Nortek Air Management and Other Industrial reporting segments. Contracts where hedge accounting was applied had a fair value liability as at 31 December 2020 of £5 million (31 December 2019: asset of £2 million). These contracts all mature between January 2021 and November 2023.

The change in fair value of foreign exchange forward contracts recognised in derivative losses on hedging relationships within Other Comprehensive Income was a charge of £16 million (2019: credit of £1 million) and a loss of £6 million (2019: £nil) was reclassified to the Income Statement.

Cross-currency swaps are designated as net investment hedges. The critical terms of the hedges are not perfectly matched against the hedged item in terms of the cost of hedging; this gives rise to ineffectiveness through the Income Statement for the year ended 31 December 2020, and could also do so in future reporting periods.

In respect of the cross-currency swaps designated as net investment hedges, for the year ended 31 December 2020, £5 million (2019: £7 million) was booked through the Income Statement in finance costs, of which a charge of £2 million (2019: credit of £1 million) was reclassified to the Income Statement from Other Comprehensive Income and has been treated as an adjusting item (note 6). The cross-currency swaps are designated in a net investment hedge accounting relationship against US Dollar and Euro net assets of certain subsidiaries. The hedged risk of spot rate represents the significant component of the movement and therefore has been recorded in the foreign currency translation reserve (note 26).

The following table shows the maturity profile of undiscounted contracted gross cash outflows of derivative financial liabilities used to manage currency risk, being both the cross-currency swaps above and foreign exchange forward contracts used to manage transaction exchange rate risk:

	0-1 years £m	1-2 years £m	2-5 years £m	5+ years £m	Total £m
Year ended 31 December 2020					
Foreign exchange forward contracts	712	393	374	–	**1,479**
Cross-currency swaps	407	553	–	–	**960**
Year ended 31 December 2019					
Foreign exchange forward contracts	1,104	552	703	42	2,401
Cross-currency swaps	499	25	547	–	1,071

Foreign currency sensitivity analysis

Currency risks are defined by IFRS 7: "Financial instruments: Disclosures" as the risk that the fair value or future cash flows of a financial asset or liability will fluctuate because of changes in foreign exchange rates.

The following table details the transactional impact of hypothetical changes in foreign exchange rates on financial assets and liabilities at the balance sheet date, illustrating the increase/(decrease) in Group operating profit caused by a 10% strengthening of the US Dollar and Euro against Sterling compared to the year-end spot rate. The analysis assumes that all other variables, in particular other foreign currency exchange rates, remain constant. The Group operates in a range of different currencies, and those with a notable impact are noted below:

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
US Dollar	**(10)**	3
Euro	**(2)**	(3)

Notes to the Financial Statements

Continued

25. Financial instruments and risk management continued

The following table details the impact of hypothetical changes in foreign exchange rates on financial assets and liabilities at the balance sheet date, illustrating the increase/(decrease) in Group equity caused by a 10% strengthening of the US Dollar and Euro against Sterling. The analysis assumes that all other variables, in particular other foreign currency exchange rates, remain constant.

	31 December 2020 £m	31 December 2019 £m
US Dollar	**8**	15
Euro	**(7)**	–

In addition, the change in equity due to a 10% strengthening of the US Dollar against Sterling for the translation of net investment hedging instruments would be a decrease of £178 million (2019: £204 million) and for Euro, a decrease of £65 million (2019: £75 million). However, there would be no overall effect on equity because there would be an offset in the currency translation of the foreign operation.

Fair value measurements recognised in the Balance Sheet

Foreign currency forward contracts are measured using quoted forward exchange rates and yield curves derived from quoted interest rates matching the maturities of the contracts.

Interest rate swap and cross-currency swap contracts are measured using yield curves derived from quoted interest and foreign exchange rates.

Hedge accounted derivatives

The following table sets out details of the Group's material hedging instruments where hedge accounting is applied at the balance sheet date:

	Average fixed rate		Notional principal		Fair value of assets/ (liabilities)	
Hedging Instruments	**2020 %**	2019 %	**2020 £m**	2019 £m	**2020 £m**	2019 £m
Pay fixed, receive floating interest rate swaps – assets						
Within one year	**–**	0.96%	**–**	259	**–**	–
In one to two years	**–**	0.92%	**–**	223	**–**	1
In two to five years	**–**	–	**–**	–	**–**	–
Total					**–**	1
Pay fixed, receive floating interest rate swaps – liabilities						
Within one year	**1.95%**	2.04%	**1,752**	1,523	**(2)**	(18)
In one to two years	**1.98%**	2.06%	**1,876**	1,617	**–**	(13)
In two to five years	**1.94%**	2.02%	**2,079**	1,889	**(85)**	(29)
Total					**(87)**	(60)
Pay fixed, receive fixed cross-currency swaps						
Within one year	**4.82%**	4.86%	**528**	522	**–**	(1)
In one to two years	**4.82%**	4.86%	**528**	522	**(80)**	(1)
In two to five years	**–**	4.86%	**–**	522	**–**	(72)
Total					**(80)**	(74)

The Group also has cross-currency swaps designated in net investment hedge accounting relationships which convert US Dollar borrowings to Euros as discussed in the Hedge of net investments in foreign entities using loans and derivatives section of this note.

The Group is exposed to the following interest rate benchmarks within its hedge accounting relationships, which are subject to interest rate benchmark reform: GBP LIBOR, USD LIBOR, EURIBOR ("IBORs"). The hedged items are Sterling, US Dollar and Euro floating rate debt.

The Group has closely monitored the market and the output from various industry working groups managing the transition to new benchmark interest rates. This includes announcements made by LIBOR regulators (including the Financial Conduct Authority ("FCA") and the US Commodity Trading Futures Commission) regarding the transition away from LIBOR to the Sterling Overnight Indexed Average Rate ("SONIA"), Secured Overnight Financing Rate ("SOFR") and Euro Short-Term Rate ("ESTR") respectively. The FCA has made it clear that, at the end of 2021, it will no longer seek to persuade, or compel banks to submit to LIBOR.

In response to the announcements, during the year the Group commenced dialogue with its banking group in respect of IBOR reform, with the expectation that the banking facility will transition to updated referenced benchmarked rates prior to the end of 2021.

25. Financial instruments and risk management continued

Below are the details of the hedging instruments and hedged items in scope of the IFRS 9 amendments due to interest rate benchmark reform by hedge type. The terms of hedged items listed match those of the corresponding hedging instruments.

Hedge type	Instrument type	Maturing	Notional	Hedged item
Cash flow hedges	Interest rate swaps, pay Sterling fixed annually, receive 1 month GBP LIBOR	July 2021	£95 million	Sterling floating rate debt linked to LIBOR
	Interest rate swaps, pay Sterling fixed annually, receive 1 month GBP LIBOR	January 2023	Variable (£30 million – £110 million)	
	Interest rate swaps, pay US Dollar fixed annually, receive 3 month US Dollar LIBOR	July 2021	Variable ($170 million – $265 million)	US Dollar floating rate debt linked to US LIBOR
	Interest rate swaps, pay 3 month US Dollar LIBOR, receive 1 month US Dollar LIBOR	July 2021	Variable ($170 million – $265 million)	
	Interest rate swaps, pay US Dollar fixed annually, receive 1 month US Dollar LIBOR	January 2023	Variable ($1,100 million – $1,500 million)	
	Interest rate swaps, pay US Dollar fixed annually, receive 1 month US Dollar LIBOR	January 2023	Variable ($450 million – $500 million)	
	Interest rate swaps, pay Euro fixed annually, receive 1 month EURIBOR	January 2023	Variable (€160 million – €400 million)	Euro floating rate debt linked to EURIBOR
	Interest rate 0% caps, pay Euro fixed annually, receive 1 month EURIBOR	January 2023	€220 million	

The Group will continue to apply the amendments to IFRS 9 until the uncertainty arising from the interest rate benchmark reforms with respect to the timing and the amount of the underlying cash flows that the Group is exposed to ends. The Group has assumed that this uncertainty will not end until the Group's contracts that reference IBORs are amended to specify the date on which the interest rate benchmark will be replaced, the cash flows of the alternative benchmark rate and the relevant spread adjustment. This will, in part, be dependent on the introduction of fallback clauses which have yet to be added to the Group's contracts and the negotiation with lenders.

Derivative and financial assets and liabilities are presented within the Balance Sheet as:

	31 December 2020 £m	31 December 2019 £m
Non-current assets	**101**	38
Current assets	**47**	19
Non-current liabilities	**(210)**	(216)
Current liabilities	**(58)**	(106)

The change in fair value of interest rate swaps is discussed in the Finance Risk Management section.

All hedging instruments are booked in the Balance Sheet as derivative financial assets or derivative financial liabilities.

The fair value of derivative financial instruments is derived from inputs other than quoted prices that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices) and they are therefore categorised within Level 2 of the fair value hierarchy set out in IFRS 13: "Fair value measurement". The Group's policy is to recognise transfers into and out of the different fair value hierarchy levels at the date the event or change in circumstances that caused the transfer to occur. There have been no transfers between levels in the year.

The following table sets out details of the Group's material hedged items at the balance sheet date where hedge accounting is applied:

	Change in fair value for calculating ineffectiveness		Balance in translation and hedging reserve for continuing hedges		Balance in translation and hedging reserve for discontinued hedges	
	2020 £m	2019 £m	**2020 £m**	2019 £m	**2020 £m**	2019 £m
Hedged items						
Floating rate borrowings – interest risk	**28**	36	**70**	42	**7**	–
Net assets of designated investments	**3**	27	**63**	60	**–**	–

There is no balance held in cash flow hedge reserve from hedging relationships for which hedge accounting is no longer applied. During the year, at the request of one of its financial counterparties, the Group novated one of its interest rate swaps to another of its financial counterparties, which had the initial effect of leaving a £9 million debit in the translation and hedging reserve for the discontinued hedge, reducing to £7 million by 31 December 2020. The remaining value in reserves will be charged to the Income Statement over the remaining life of the cash flows to January 2023, reflecting the cash flow profile on which the hedge had been originally designated.

Notes to the Financial Statements

Continued

26. Issued share capital and reserves

Share Capital	31 December 2020 £m	31 December 2019 £m
Allotted, called-up and fully paid		
4,858,254,963 (31 December 2019: 4,858,254,963) Ordinary Shares of 48/7p each (31 December 2019: 48/7p each)	**333**	333
12,831 (31 December 2019: 12,831) 2017 Incentive Plan Shares of £1 each(1)	**–**	–
	333	333

(1) Following the crystallisation of the 2017 Incentive Plan on 31 May 2020 for £nil, the 2017 Incentive Plan shares will be re-designated as deferred shares and cancelled by the Company.

The rights associated with each class of share are described in the Directors' Report.

Merger reserve and Other reserves

The Merger reserve represents the excess of fair value over nominal value of shares issued in consideration for the acquisition of subsidiaries. Other reserves comprise accumulated adjustments in respect of Group reconstructions.

Translation and hedging reserve

In order to provide useful information about the Group's hedging arrangements, the translation reserve and hedging reserve are combined. Including the different components of hedging in one place enables a clearer explanation of the three components of hedging. These components are disaggregated below with movements within Other Comprehensive Income during the year shown below and further explanation provided in note 25.

	Cost of hedge reserve £m	Cash flow hedge reserve £m	Foreign currency translation reserve £m	Translation and hedging reserve £m
At 1 January 2019	(6)	(5)	506	495
Movements within other comprehensive income/(expense):				
Retranslation of net assets	–	–	(451)	(451)
Foreign exchange differences on borrowings hedging net assets	–	–	83	83
Associated deferred tax	–	–	(3)	(3)
Change in fair value of derivatives designated in net investment hedges	–	–	19	19
Associated deferred tax	–	–	(22)	(22)
Change in fair value of derivatives designated in cash flow hedges	–	(35)	–	(35)
Amounts reclassified to the Income Statement	–	–	(13)	(13)
Associated deferred tax	–	6	–	6
Net movement in cost of hedging	(1)	–	–	(1)
At 31 December 2019	(7)	(34)	119	78
Movements within other comprehensive income/(expense):				
Retranslation of net assets	–	–	(87)	(87)
Foreign exchange differences on borrowings hedging net assets	–	–	61	61
Associated deferred tax	–	–	–	–
Change in fair value of derivatives designated in net investment hedges	–	–	(55)	(55)
Associated deferred tax	–	–	–	–
Change in fair value of derivatives designated in cash flow hedges	–	(44)	–	(44)
Associated deferred tax	–	9	–	9
Amounts reclassified to the Income Statement	(1)	6	3	8
At 31 December 2020	**(8)**	**(63)**	**41**	**(30)**

The cash flow hedge reserve represents the cumulative fair value gains and losses on derivatives for which cash flow hedge accounting has been applied. Movements and balances on derivatives designated in net investment hedges are shown as part of the foreign currency translation reserve.

The foreign currency translation reserve contains exchange differences on the translation of subsidiaries with a functional currency other than Sterling, together with gains and losses on the translation of liabilities and cumulative fair value gains and losses on derivatives that hedge the Company's net investment in foreign subsidiaries.

27. Cash flow statement

	Notes	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Reconciliation of operating (loss)/profit to net cash from operating activities generated by continuing operations			
Operating (loss)/profit		**(338)**	318
Adjusting items	6	**678**	784
Adjusted operating profit	6	**340**	1,102
Adjustments for:			
Depreciation of property, plant and equipment		**435**	434
Amortisation of computer software and development costs		**57**	64
Share of adjusted operating profit of equity accounted investments	15	**(62)**	(66)
Restructuring costs paid and movements in provisions		**(150)**	(320)
Defined benefit pension contributions paid(1)		**(111)**	(183)
Change in inventories		**187**	(12)
Change in receivables		**250**	72
Change in payables		**(13)**	(2)
Acquisition costs and associated transaction taxes		**–**	(16)
Tax paid		**–**	(117)
Interest paid on loans and borrowings		**(144)**	(166)
Interest paid on lease obligations		**(21)**	(21)
Net cash from operating activities		**768**	769

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

Reconciliation of cash and cash equivalents, net of bank overdrafts	31 December 2020 £m	31 December 2019 £m
Cash and cash equivalents per Balance Sheet	**311**	512
Bank overdrafts included within current interest-bearing loans and borrowings (note 20)	**(151)**	(195)
Cash and cash equivalents, net of bank overdrafts per Statement of Cash Flows	**160**	317

Cash flow information relating to discontinued operations is as follows:

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

Net debt reconciliation

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

Notes to the Financial Statements
Continued

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

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

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

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

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

28. Commitments
Amounts payable under lease obligations:

Minimum lease payments	31 December 2020 £m	31 December 2019 £m
Amounts payable:		
Within one year	**101**	91
After one year but within five years	**239**	235
Over five years	**325**	375
Less: future finance charges	**(110)**	(119)
Present value of lease obligations	**555**	582
Analysed as:		
Amounts due for settlement within one year	**81**	71
Amount due for settlement after one year	**474**	511
Present value of lease obligations	**555**	582

It is the Group's policy to lease certain of its property, plant and equipment. The average lease term is 10 years. Interest rates are fixed at the contract date. All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments.

The Group's obligations under lease arrangements are secured by the lessors' rights over the leased assets.

Certain leases within the Group contain extension or termination options to allow for flexibility within these lease agreements. Where these options are not reasonably certain to be exercised they are not included in the lease obligation. The value of these associated undiscounted cash flows is £277 million.

28. Commitments continued
The table below shows the key components in the movement in lease obligations.

	£m
At 31 December 2019	582
Additions	56
Interest charge	21
Reassessment of lease obligation	14
Payment of principal	(76)
Payment of interest	(21)
Disposals	(20)
Exchange adjustments	(1)
At 31 December 2020	**555**

Capital commitments
At 31 December 2020, there were commitments of £106 million (31 December 2019: £164 million) relating to the acquisition of new plant and machinery.

29. Related parties
Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note. Sales to and purchases from Group companies are priced on an arm's length basis and generally are settled on 30 day terms.

In the ordinary course of business sales and purchases of goods take place between subsidiaries and equity accounted investment companies priced on an arm's length basis. Sales by subsidiaries to equity accounted investments in the year ended 31 December 2020 totalled £23 million (2019: £12 million). Purchases by subsidiaries from equity accounted investments in the year ended 31 December 2020 totalled £7 million (2019: £7 million). At 31 December 2020, amounts receivable from equity accounted investments totalled £9 million (31 December 2019: £5 million) and amounts payable to equity accounted investments totalled £1 million (31 December 2019: £1 million).

Remuneration of key management personnel
The remuneration of the Directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS 24: "Related party disclosures". Further information about the remuneration of individual Directors is provided in the audited part of the Directors' Remuneration report on pages 114 and 123.

	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Short-term employee benefits	**3**	4
Share-based payments	**7**	9
	10	13

30. Contingent liabilities
As a result of acquisitions made by the Group, certain contingent legal and warranty liabilities have been identified as part of the fair value review of these acquisition balance sheets. Whilst it is difficult to reasonably estimate the timing and ultimate outcome of these claims, the Directors' best estimate has been included in the Balance Sheet where they existed at the time of acquisition and hence were recognised in accordance with IFRS 3: "Business combinations". Where a provision has been recognised, information regarding the different categories of such liabilities and the amount and timing of outflows is included within note 21.

Given the nature of the Group's business many of the Group's products have a large installed base, and any recalls or reworks related to such products could be particularly costly. The costs of product recalls or reworks are not always covered by insurance. Recalls or reworks may have a material adverse effect on the Group's financial condition, results of operations and cash flows.

The Group has contingent liabilities representing guarantees and contract bonds given in the ordinary course of business on behalf of trading subsidiaries. No losses are anticipated to arise on these contingent liabilities. The Group does not have any other significant contingent liabilities.

Company Balance Sheet for Melrose Industries PLC

	Notes	31 December 2020 £m	31 December 2019 £m
Fixed assets			
Investment in subsidiaries	3	**10,579**	10,573
Debtors:			
Amounts falling due within one year	4	**425**	413
Amounts falling due after one year	4	**29**	25
Creditors:			
Amounts falling due within one year	5	**(2,041)**	(2,016)
Net current liabilities		**(1,587)**	(1,578)
Total assets less current liabilities		**8,992**	8,995
Provisions	6	**(1)**	(3)
Net assets		**8,991**	8,992
Capital and reserves			
Issued share capital	7	**333**	333
Share premium account		**8,138**	8,138
Merger reserve		**109**	109
Retained earnings		**411**	412
Shareholders' funds		**8,991**	8,992

The Company reported a loss for the financial year ended 31 December 2020 of £15 million (2019: loss of £10 million).

The financial statements were approved by the Board of Directors on 4 March 2021 and were signed on its behalf by:

Geoffrey Martin
Group Finance Director

4 March 2021

Simon Peckham
Chief Executive

4 March 2021

Registered number: 09800044

Company Statement of Changes in Equity

	Issued share capital £m	Share premium account £m	Merger reserve £m	Retained earnings £m	Shareholders' funds £m
At 1 January 2019	333	8,138	109	640	9,220
Loss for the year (note 2)	–	–	–	(10)	(10)
Total comprehensive expense	–	–	–	(10)	(10)
Dividends paid	–	–	–	(231)	(231)
Equity-settled share-based payments	–	–	–	13	13
At 31 December 2019	333	8,138	109	412	8,992
Loss for the year (note 2)	–	–	–	(15)	(15)
Total comprehensive expense	–	–	–	(15)	(15)
Equity-settled share-based payments	–	–	–	14	14
At 31 December 2020	**333**	**8,138**	**109**	**411**	**8,991**

Refer to the Section 172 statement in the Strategic Report on pages 54 to 57 for further details on the Company's Distribution Policy.

Notes to the Company Balance Sheet

1. Significant accounting policies

Basis of accounting

Melrose Industries PLC ("the Company") is a public company limited by shares. The Company is incorporated in the United Kingdom under the Companies Act 2006 and registered in England and Wales. The address of the registered office is given on the back cover. The nature of the Group's operations and its principal activities are set out in the Strategic Report on pages 1 to 87.

The Financial Statements have been prepared under the historical cost convention and in accordance with Financial Reporting Standard 102 (FRS 102) issued by the Financial Reporting Council.

The functional currency of Melrose Industries PLC is considered to be pounds Sterling because that is the currency of the primary economic environment in which the Company operates.

Melrose Industries PLC meets the definition of a qualifying entity under FRS 102 and has therefore taken advantage of the disclosure exemptions available to it in respect of its separate Financial Statements. Melrose Industries PLC is consolidated in its Group Financial Statements. Exemptions have been taken in these separate Company Financial Statements in relation to share-based payments, presentation of a cash flow statement, the remuneration of key management personnel and financial instruments.

The principal accounting policies are consistent with the prior year and are summarised below.

Going concern

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

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

Covenants

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

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

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

Testing

The Group has modelled two scenarios in its assessment of going concern; a base case and a reasonably possible sensitised case.

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

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

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

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

Investments

Investments in subsidiaries are measured at cost less impairment.

For investments in subsidiaries acquired for consideration including the issue of shares qualifying for merger relief, cost is measured by reference to the nominal value of the shares issued plus fair value of other consideration. Any premium is ignored.

Impairment of assets

Assets are assessed for indicators of impairment at each balance sheet date. If there is objective evidence of impairment, an impairment loss is recognised in profit or loss as described below.

Notes to the Company Balance Sheet
Continued

1. Significant accounting policies continued

Non-financial assets
An asset is impaired where there is objective evidence that, as a result of one or more events that occurred after initial recognition, the estimated recoverable value of the asset has been reduced. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

Where indicators exist for a decrease in impairment loss, the prior impairment loss is tested to determine reversal. An impairment loss is reversed on an individual impaired asset to the extent that the revised recoverable value does not lead to a revised carrying amount higher than the carrying value had no impairment been recognised.

Financial instruments
Financial assets and financial liabilities are recognised when the Company becomes a party to the contractual provisions of the instrument. Financial liabilities are classified according to the substance of the contractual arrangements entered into.

Financial assets and liabilities
All financial assets and liabilities are initially measured at transaction price (including transaction costs).

Financial assets and liabilities are only offset in the Balance Sheet when, and only when, there exists a legally enforceable right to set off the recognised amounts and the Company intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Financial assets are derecognised when, and only when, a) the contractual rights to the cash flows from the financial asset expire or are settled, b) the Company transfers to another party substantially all of the risks and rewards of ownership of the financial asset, or c) the Company, despite having retained some, but not all, significant risks and rewards of ownership, has transferred control of the asset to another party.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged, cancelled or expires.

Share-based payments
The Company issues equity-settled share-based payments to certain employees. The required disclosures are included in the Group Consolidated Financial Statements.

Equity-settled share-based payments are measured at fair value (excluding the effect of non-market based vesting conditions) at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Company's estimate of the shares that will eventually vest and adjusted for the effect of non-market based vesting conditions.

Fair value is measured by use of the Black-Scholes pricing model. The expected life used in the model has been adjusted, based on the Directors' best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

Where equity-settled share-based payments are made available to employees of the Company's subsidiaries, these are treated as increases in equity over the vesting period of the award with a corresponding increase in the Company's investment in subsidiaries.

Taxation
Current tax, including UK corporation tax and foreign tax, is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred. Timing differences are differences between the Company's taxable profits and its results as stated in the Financial Statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the Financial Statements.

Provisions
Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a rate that reflects the current market assessment of the time value of money and, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

Critical accounting judgements and key sources of estimation uncertainty
There were no critical accounting judgements that would have a significant effect on the amounts recognised in the Parent Company Financial Statements or key sources of estimation uncertainty at the balance sheet date that would have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

2. Result for the year
As permitted by section 408 of the Companies Act 2006 the Company has elected not to present its own Profit and Loss Account for the year. Melrose Industries PLC reported a loss for the financial year ended 31 December 2020 of £15 million (2019: loss of £10 million).

The auditor's remuneration for audit services to the Company is disclosed in note 7 to the Group Consolidated Financial Statements.

Directors' remuneration is disclosed in the Directors' Remuneration report on pages 110 to 126. There were no other employees of the Company in the year.

3. Investment in subsidiaries

	£m
At 1 January 2020	10,573
Additions	6
At 31 December 2020	**10,579**

A £6 million investment from equity-settled share-based payments for subsidiaries is included as an addition to investments in subsidiaries at 31 December 2020. Further details on the Group's share-based payment schemes are included in note 23 to the Group Consolidated Financial Statements.

3. Investment in subsidiaries continued
The Company evaluates its investments in subsidiary undertakings annually for any indicators of impairment. The Company considers the relationship between its market capitalisation and the carrying value of its investments, among other factors, when reviewing for indicators of impairment. As at 31 December 2020, the market capitalisation of the Company of £8,650 million was below the carrying value of its investment (£10,579 million) net of intercompany positions (£1,616 million) indicating a potential impairment, along with the pervasive impact of COVID-19 on certain of the Group's businesses.

The recoverable amount of the investment has been determined using the information set out in Note 11 to the Group Consolidated Financial Statements and is in excess of its carrying value.

The following subsidiaries and significant holdings were owned by the Company as at 31 December 2020:

	Equity interest %	Class of Share held
Argentina		
Avenida Del Libertador 602, 4' Piso, Buenos Aires		
Transmisiones Homocineticas Argentinas SA *(in liquidation)*	49	Ordinary B[1]
Australia		
Unit 6, 256-258 Leitchs Road, Brendale, Queensland, 4500		
Bristol Meci Australasia Pty Limited	100	Ordinary
Hawker Siddeley Switchgear Pty Limited	100	Ordinary
45-49 McNaughton Road, Clayton Victoria, 3168		
Unidrive Pty Ltd *(in liquidation)*	100	Ordinary
Level 16, 201 Elizabeth Street, Sydney, NSW 2000		
Ergotron Australia Pty Ltd	100	Ordinary
Belgium		
Robert Klingstraat 96 box A, 8940 Wervik		
Nortek Global HVAC Belgium NV	100	Ordinary
Brazil		
Cicada de Vitoria, Estado do Espirio Santo, na Av. Nossa, Senhora da Penha, 520, Sala 404, Praia do Canto, 29055-131		
Nordyne do Brasil Participações Ltda	100	Common
Av. Alfredo Ignácio Noqueira Penido, 335 – Sala 1103 – Edifício Madison Power, São José dos Campos, SP, 12246-000		
GKN Aerospace Transparency Systems do Brasil Ltda	100	Quota capital
Rua Joaquim Silveira 557, Parque Sao Sebastiao, 91060-320 Porto Alegre, RS		
GKN do Brasil Ltda	100	Common
Av. da Emancipacao no. 4.500, CEP 13.184-542, Bairro Santa Esmeralda, Hortolandia, Sao Paulo		
GKN Sinter Metals Ltda	100	Common
British Virgin Islands		
Commerce House, Wickhams Cay 1, P.O. Box 3140, Road Town, Tortola VG1110		
Nortek Trading Limited	100	Ordinary
Canada		
600-1134 Grande Allée Ouest, Quebec, G1S 1E5		
Brush Canada Services Inc./Services Brush Canada Inc.	100	Common stock
Fokker Elmo Canada Inc.	100	Ordinary
Innergy Tech, Inc.	100	Ordinary
Nortek Air Solutions Quebec, Inc	100	Ordinary
44 Chipman Hill Suite 1000 Saint John, New Brunswick E2L 2A9		
2GIG Technologies Canada, Inc.	100	Class A Common
Queen's Marque 600-1741 Lower Water Street, Halifax, N.S. B3J 0J2		
Ergotron Canada Corporation	100	Ordinary
3489 Allan Dr SW, Edmonton AB T6W 3GS		
Venmar Ventilation ULC	100	Common Class A Special
1500-1874 Scarth Street, Regina, Saskatchewan, S4P 4E9		
Nortek Air Solutions Canada, Inc.	100	Ordinary
7 Michigan Boulevard, St. Thomas, Ontario		
GKN Sinter Metals – St. Thomas, Ltd.	100	Common stock
China		
Room 1108, Binjiang International Building, No.88 Tonggang Road, Changshu Economic and Technological Development Zone, Jiangsu Province, 21550		
Brush Electrical Machines (Changshu) Co. Limited	100	Registered investment
2025, 2031 2nd Floor, Tower C., 155 West Fute Road, Waigaoqi Bonded Zone Shanghai, 200131		
FKI Engineering Shanghai Limited	100	Ordinary
No. 6 Zone, Daxin Group, Zhongkai Hi-tech District, Huizhou		
Guangdong Broan IAQ Systems Co. Limited	100	Ordinary
The 3rd Industry Area, Juzhou Shijie, Dongguan, Guangdong, 523290		
Dongguan Ergotron Precision Technology Co Limited	100	Registered investment
Room 2913 and 2914, Taiwan Merchants Building, 11th Dongguan Avenue, Dongcheng, Dongguan, Guangdong Province		
Dongguan Ergotron Precision Technology Design Services Co., Limited	100	Registered investment
Unit 1801-1809, Tower 2, Kingliton Financial Center, No. 1100 Xingye Road, Haiwang Community, Xin'an Sub-district, Baoan District, Shenzhen		
Linear Electronics (Shenzhen) Limited	100	Ordinary

Notes to the Company Balance Sheet
Continued

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
Room 22D2, 22D3, No.895 South Yan'an Rd, Changning District, Shanghai		
Nortek (Shanghai) Trading Co Limited	100	Ordinary
No 71 Xiangyun Road, Langfang Economic & Technical Development Zone, Langfang		
Fokker Elmo (Langfang) Electrical Systems Co. Ltd	100	Registered investment
On the north of 1500 meters, Wuping Dong Road, Shengfang Town, Bazhou City, Hebei Province		
GKN (Bazhou) Metal Powder Company Limited	40	Registered investment
Unit A, 6/F, Building A1#, No. 2555 Xiupu Road, Pudong New Area, Shanghai, 201315		
GKN China Holding Co Ltd	100	Registered investment
18 North Shitan Road, North Industrial Park, Development Zone, Danyang, Jiangsu, 212310		
GKN Danyang Industries Company Limited	100	Registered investment
No. 1 Cuigu, Northern New Zone, Chongqing, 401122		
GKN HUAYU Driveline Systems (Chongqing) Co. Ltd	9	Ordinary
1 Xinwang Road, Jingjiang Economic and Technic Development Zone, Jingjiang, Jiangsu		
GKN Aerospace (Jingjiang) Co., Ltd	100	Registered investment
No.8 Kangmin Road, Yizheng		
GKN Sinter Metals Yizheng Co Ltd	100	Registered investment
Xiguo Industrial Zone, Mengzhou City, Henan Province, 454750		
GKN Zhongyuan Cylinder Liner Company Limited	59	Registered investment
Zijin Kechuang Center 4 Level, 416 Room, Economy Development Zone, Lishui, Nanjing		
Nanjing FAYN Piston Ring Company Limited	19.79	Registered investment
898 Kangshen Road, Pudong, Shanghai		
Shanghai GKN Driveline Sales Co Ltd	49	Ordinary
950 KangQiao Road, Pudong New Area, Shanghai		
Shanghai GKN HUAYU Driveline Systems Company Limited	50	Registered investment
Room 805, 8th floor, Building 2, No. 1859, Shibo Avenue, Shanghai		
GKN Aerospace (Shanghai) Co., Ltd	100	Ordinary
Colombia		
1301, 13/F Bank of America Tower, 12 Harcourt Road, Central		
MiOS Colombia *(in liquidation)*	42	Ordinary
Calle 32 No. 15 – 23 Barrio Rincon de Girón, Girón Santander		
Transejes Transmisiones Homocineticas de Colombia SA	49	Ordinary
Czech Republic		
Edvarda Beneše 564/39, Doudlevce, 301 00 Plzen		
Brush SEM s.r.o.	100	Ordinary
France		
Boulevard De L Europe, BP 177 91006 Evry-Courcouronnes CEDEX		
Arianespace Participation S.A.	1.6110	Ordinary
12 Quai du Commerce 69009 Lyon		
Ergotron France SARL	100	Ordinary
ZI de Rosarge, 230 Rue de la Dombes, Les Echets, 01700, Mirabel		
Nortek Global HVAC France SAS	100	Ordinary
7 rue de la Briqueterie, 02240 Ribemont		
GKN Driveline Ribemont SARL	100	Ordinary
100 Avenue Vanderbilt, 78955 Carrieres-sous-Poissy		
GKN Automotive SAS	100	Ordinary
GKN Driveline SA	99.99	Ordinary
GKN Freight Services EURL	100	Ordinary
765 rue Albert Einstein, CS 70402, 13591 Aix-en-Provence Cedex 3		
NH Industries SAS	5.5	Ordinary
20 rue Lavoisier, 95300 Pontoise		
GKN Aerospace France SARL	100	Ordinary
Germany		
c/o Meier & Collegen GmbH, Teichhorn 4-6, 24119, Kronshagen		
Ergotron Deutschland GmbH	100	Ordinary
Brunhamstr. 21, 81249, Munich		
GKN Aerospace Deutschland GmbH	100	Ordinary
Carl-Legien-Strasse 10, 63073 Offenbach am Main		
GKN Driveline Deutschland GmbH	100	Ordinary
Hauptstrasse 130, 53797 Lohmar		
GKN Driveline International GmbH	100	Ordinary
Hafenstrasse 41, 54293 Trier		
GKN Driveline Trier GmbH	100	Ordinary
Nussbaumweg 19-21 51503, Rosrath		
GKN Driveline Service GmbH	100	Ordinary
Opelkreisel 1-9, 67663 Kaiserslautern		
GKN Gelenkwellenwerk Kaiserslautern GmbH	100	Ordinary
Krebsoege 10, 42477 Radevormwald		
GKN Powder Metallurgy Holding GmbH	100	Ordinary
GKN Sinter Metals Engineering GmbH	100	Ordinary

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
Pennefeldsweg 11-15, 53177, Bonn		
GKN Sinter Metals Components GmbH	100	Ordinary
Dahlienstrasse 43, 42477 Radevormwald		
GKN Sinter Metals Filters GmbH Radevormwald	100	Ordinary
Industriestr. 1, 97769 Bad Brückenau		
GKN Sinter Metals & Forge Operations GmbH	100	Ordinary
Am Fliegerhorst 9, 99947 Bad Langensalza		
GKN Sinter Metals GmbH, Bad Langensalza	100	Ordinary
Peterstrasse 69, 42499, Hueckeswagen		
Hoeganaes Corporation Europe GmbH	100	Ordinary
Hong Kong		
31/F, Tower Two, Times Square, 1 Matheson Street, Causeway Bay		
Linear HK Manufacturing Limited	100	Ordinary
Citicorp Centre, STE 1607-8, 18 Whitfield Road, Causeway Bay		
MiOS Limited *(in liquidation)*	42	Ordinary
India		
Block 2A No. 311, NPR Complex. Survey No 197, Hoody Village, K R Puram Hobli, Whitefield Road, Bangalore - 560048, Karnataka		
Fokker Elmo SASMOS Interconnection Systems Limited	49	Ordinary
270, Sector-24, Faridabad 121 005, Haryana		
GKN Driveline (India) Limited	97.03	Ordinary
146 Mumbai Pune Road, Pimpri, Pune 411 018		
GKN Sinter Metals Private Limited	100	Ordinary
Shop No. 002, Lumkad Sky Vista, S. No. 230/AViman Naga/3/2, Viman Nagar, Pune, Maharashtra, 411014		
GKN Fokker Elmo India Private Limited	100	Ordinary
135, 2nd Floor, RMZ Titanium, Old Airport Road, Bengaluru, 560 017		
GKN Aerospace Engine Systems India Private Limited	100	Ordinary
Office No. 301-308, 3rd Floor, Pride Silicon Plaza Survey No 106A, Nr Chaturshringi Temple, S.B. Road, Pune, Maharashtra, 411016		
IntelliVision Technologies Private Limited	99.99	Ordinary
Ireland		
3rd Floor, Kilmore House, Park Lane, Spencer Dock, Dublin 1		
Nortek Air Solutions (Ireland) Limited	100	Ordinary
Isle of Man		
c/o Willis Management (Isle of Man) Ltd, Tower House, Loch Promenade, Douglas, IM1 2LZ		
Ipsley Insurance Limited	100	Ordinary
Italy		
Via dei Campi della Rienza 8, 39031 Brunico, BZ		
GKN Driveline Brunico SpA	100	Ordinary
GKN Italia SpA	100	Ordinary
Via Fratelli Cervi 1, 50013 Campi Bisenzio, FI		
GKN Driveline Firenze SpA	100	Ordinary
Via Delle Fabbriche 5, 39031 Brunico, BZ, Italy		
GKN Sinter Metals SpA	100	Ordinary
Japan		
Tokyo Club Building 11F, 3-2-6 Kasumigaseki, Chiyoda-ku, Tokyo 100-0013		
Ergotron Japan KK	100	Ordinary
2388 Ohmiya-cho, Tochigi City, 328-8502 Tochigi		
GKN Driveline Japan Ltd	100	Ordinary
GKN Driveline Tochigi Holdings KK	100	Ordinary
Senri Life Science Centre Building. 12F, 1-4-2 Shin Senri Higashi-machi, Toyonaka-shi, Osaka		
GKN Powder Metallurgy Japan K.K.	100	Ordinary
Jersey		
JTC House, 28 The Esplanade, St. Helier, JE2 3QA		
GKN Finance Limited	100	Ordinary
Korea		
53 3Gongdan2-ro, Seobuk-gu, CheonAn-si, Chungcheongnam-do		
GKN Driveline Korea Limited	100	Common stock
Malaysia		
10th Floor, Menara Hap Seng, No.1 & 3, Jalan P. Ramless, 50250 Kuala Lumpur		
GKN Engine Systems Component Repair Sdn Bhd.	100	Ordinary
Suite A, Level 9, Wawasan Open University, 54, Jalan Sultan Ahmad Shah, Georgetown, Pulau, 10050, Penang		
GKN Driveline Malaysia Sdn Bhd	68.42	Ordinary
Malta		
A18b, Industrial Estate, Marsa, 3000		
Mediterranean Power Electric Company Limited	26	A Ordinary[3]

Notes to the Company Balance Sheet
Continued

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
Mexico		
Calle Vinedos 4500, Parque Industrial El Bajio, Tecate, Baja California, 21430		
Broan Building Products-Mexico S de RL de CV	100	Registered investment
Calle Washinton 3701, interior 18, Complejo Industrial Las Americas, Chihuahua, Chihuahua, C.P. 31114		
FAE Aerostructures SA de CV	100	Ordinary
Av. CFE No. 709, Parque Industrial Millennium, San Luis Potosi S.L.P 78395		
GKN Aerospace San Luis Potosi S. de R.L. de C.V. *(in liquidation)*	100	Fixed equity
Carretera Panamericana km 284, Celaya, Guanajuato, C.P. 38110		
GKN Driveline Celaya SA de CV	99.86	Ordinary
GKN Driveline Mexico Services SA de CV	98	Ordinary
GKN Driveline Mexico Trading SA de CV	98	Ordinary
Carretera Alterna Celaya Villagrán Km 11, Col. El Pintor, Villagrán, Guanajuato, C.P. 38260		
GKN Driveline Villagran SA de CV	98	Ordinary
Av. Constituyentes Pte. 206, int 607 B, col., El Jacal, Queretaro, C.P. 76187		
GKN Sinter Metals Mexico S. De. R.L. De. C.V.	100	Membership interest
GKN Sinter Metals Mexico (Services) S. De. R.L. De. C.V.	100	Membership interest
Calle Profesor Rodolfo Gonzalez 100, Colonia Jardines de la Victoria, Guadalupe, Nuevo Leon, CP 67119		
Manufactura e Innovacion Monterrey, S. de R.L. de C.V.	100	Membership interest
Avenida San Angel 240, numero interior 2, Colonia Valle San Agustin, C.P. 25215, Coahulia de Zaragoza		
Manufacturas Avanzadas Ramsal, S. de. R.L. de C.V.	100	Membership interest
The Netherlands		
Beeldschermweg 3, 3821 AH Amersfoort		
Ergotron Nederland BV	100	Ordinary
Schaardijk 372 5th Floor, Building 2 2909LA Capelle aan den Ijssel		
Brush HMA BV	100	Ordinary
Luna Arena, Herikerbergweg 238, 1101 CM, Amsterdam		
Nortek Holding BV	100	Ordinary
Nortek International Holdings BV	100	Ordinary
Ridderkerk Property 1 BV	100	Ordinary
Aviolandalaan 37, 4631 RP, Hoogerheide		
Business Park Aviolanda B.V.	20	Ordinary
Markt 22, 3351 PB, Papendrecht		
Fabriek Slobbengors Beheer B.V.	49	Ordinary
Fabriek Slobbengors C.V.	49	Ordinary[4]
Hoofdkantoor Slobbengors Beheer B.V.	49	Ordinary
Kantoor Industrieweg C.V.	49	Ordinary
Aviolandalaan 31, 4631 RP, Hoogerheide		
Fokker Aircraft Services B.V.	100	Ordinary
Fokker Techniek BV	100	Ordinary
Aviolandalaan 33, Hoogerheide, 4631 RP		
Fokker Elmo B.V.	100	Ordinary
Grasbeemd 28, 5705 DG, Helmond		
Fokker Landing Gear B.V.	100	A Ordinary
Industrieweg 4, 3351 LB, Papendrecht		
Cooperative Delivery of Retrokits (CDR) V.O.F.	50	Ordinary
Fokker Procurement Combination B.V.	100	Ordinary
Structural Laminates Industries B.V.	100	Ordinary
Fokker Technologies Group B.V.	100	Ordinary
Fokker Technologies Holding B.V.	100	Ordinary
Fokker Technology B.V.	100	Ordinary
GKN Aerospace Netherlands B.V.	100	Ordinary
Fokker Engineers & Contractors B.V.	100	Ordinary
Fokker Aerospace B.V.	100	Ordinary
Fokker Aerostructures B.V.	100	Ordinary
Fokker (CDR) B.V.	100	Ordinary
Hoeksteen 40, 2132 MS, Hoofddorp		
Fokker Services B.V.	100	Ordinary
11th Floor, The Colmore Building, 20 Colmore Circus Queensway, Birmingham, B4 6AT		
GKN UK Holdings BV	100	Ordinary
Norway		
Kirkegårdsveien 45, 3616 Kongsberg		
GKN Aerospace Norway AS	100	Ordinary
Kongsberg Technology Training Centre AS	33.33	Ordinary
Kongsberg Terotech AS	50	Ordinary
Oman		
Street 14, Nizwa Industrial Estate, P.O Box 1896 PC112, Ruwi		
Brush Middle East LLC	70	Membership interest

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
Poland		
Ul. B. Krzywoustego 31 G, 56-400 Oleśnica,		
GKN Driveline Polska Sp z o o	100	Ordinary
Portugal		
Avenida Marechal Gomes da Costa, 1131, 4150-360, Porto		
GKN Automotive Portugal, Limitada	100	Quota
Romania		
Str. Condorilor 9, 600302, Bacau		
FOAR S.R.L.	49	Ordinary
Hermes Business Campus, Dimitrie Pompeiu Blvd 5-7, Building 2, 3rd floor Bucharest 020337 RO, Bucureşti 077190		
Fokker Engineering Romania S.R.L.	100	Ordinary
33 Urziceni Street, Buzau 120226		
Hoeganaes Corporation Europe SA	100	Ordinary
Russian Federation		
Nizhniy Novgorod, 77 Ulitsa Gorkogo, Premises P6		
IntelliVision Limited	100	Ordinary
Saudi Arabia		
P.O. Box 2091, Riyadh 11451		
Huntair Arabia	49	Ordinary
Singapore		
1800 West Camp Road, Seletar Aerospace Park		
Fokker Services Asia Pte Ltd	100	Ordinary
38 Beach Road #29-11, South Beach Tower, 189767		
Nortek Air Solutions Pte. Ltd	100	Ordinary
Slovenia		
Rudniska cesta 20, Zrece 3214		
GKN Driveline Slovenija d o o	100	Ordinary
Spain		
Pol. Ind. Can Salvatella, Avenida Arrahona 54-56, 08210 Barbera del Valles, Barcelona		
GKN Ayra Servicio, SA	100	Ordinary
Avenida de Citroen s/n, 36210 Vigo		
GKN Driveline Vigo, SA	100	Ordinary
Sagarbidea 2, 20750 Zumaia		
GKN Driveline Zumaia, SA	100	Ordinary
Polígono Industrial s/n, Maçanet de la Selva, 17412 Girona		
Stork Prints Iberia SA	100	Ordinary
Sweden		
SE - 461 81, Trollhättan		
GKN Aerospace Sweden AB	100	Ordinary
GKN Sweden Holdings AB	100	Ordinary
SE - 731 36, Köping		
GKN Driveline Köping AB	100	Ordinary
BRÖDERNA UGGLAS GATA, SE - 58254 Linköping		
Industrigruppen JAS AB	20	Ordinary
Taiwan		
14 Kwang Fu Road, Hsin-Chu Industrial Park, Hukou, Hsin Chu 30351		
Taiway Limited	36.25	Common stock
Thailand		
9/21 Moo 5, Phaholyothin Road Klong 1, Klong Luang, Patumthanee, 12120		
GKN Aerospace Transparency Systems (Thailand) Limited	100	Ordinary
Eastern Seaboard Industrial Estate, 64/9 Moo 4, Tambon Pluakdaeng, Amphur Pluakdaeng, Rayong 21140		
GKN Driveline (Thailand) Limited	100	Ordinary
GKN Driveline Manufacturing Ltd *(In liquidation)*	100	Ordinary
Turkey		
Ege Serbest Bölgesi, SADI Sok. No:10, 35410 Gaziemir, Izmir		
Fokker Elmo Havacilik Sanayi Ve Ticaret Limited Sirketi	100	Ordinary
Organize Sanayi Bolgesi 20, Cadde No: 17, 26110, Eskisehir		
GKN Eskisehir Automotive Products Manufacture and Sales A.S.	100	Ordinary
Yakuplu Mah. Haramidere Sanayi Sitesi, J Blok, No. 106-107-108, Beylikdüzü, Istanbul		
GKN Sinter Istanbul Metal Sanayi Ve Ticaret Anonim Şirketi	100	Ordinary
United Kingdom		
11th Floor, The Colmore Building, 20 Colmore Circus Queensway, Birmingham, B4 6AT		
Alcester Capricorn	100	Ordinary
Alcester EP1 Limited	100	Ordinary
Alcester Number 1 Limited	100	Ordinary
Alder Miles Druce Limited	100	Ordinary
Ambi-Rad Group Limited	100	Ordinary

Notes to the Company Balance Sheet
Continued

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
Ball Components Limited	100	Ordinary
Birfield Limited	100	Ordinary
British Hovercraft Corporation Limited	100	Ordinary
Brush Electrical Engineering Company Limited	100	Ordinary
Brush Electrical Machines Limited	100	Ordinary
Brush Holdings Limited	100	Ordinary
Brush Properties Limited	100	Ordinary
Brush Scheme Trustees Limited	100	Ordinary
Brush Switchgear Limited	100	Ordinary
Brush Transformers Limited	100	Ordinary
Colmore Lifting Limited	100	Ordinary
Colmore Overseas Holdings Limited	100	Ordinary
Danks Holdings Limited	100	Ordinary
Eachairn Aerospace Holdings Limited	100	Ordinary
Eaton-Williams Holdings Limited	100	Ordinary
Ergotron (UK) Limited	100	Ordinary
FAD (UK) Limited	100	Ordinary
Falcon Works Property Limited	100	Ordinary
Firth Cleveland Limited	100	Ordinary
FKI Plan Trustees Limited	100	Ordinary
F.P.T. Industries Limited	100	Ordinary
GKN Aerospace Holdings Limited	100	Ordinary
GKN Aerospace Transparency Systems (Kings Norton) Limited	100	Ordinary
GKN Aerospace Transparency Systems (Luton) Limited	100	Ordinary
GKN Automotive Holdings Limited	100	Ordinary
GKN Birfield Extrusions Limited	100	Ordinary
GKN Bound Brook Limited	100	Ordinary
GKN Building Services Europe Limited	100	Ordinary
GKN CEDU Limited	100	Ordinary
GKN Composites Limited	100	Ordinary
GKN Computer Services Limited	100	Ordinary
GKN Countertrade Limited	100	Ordinary
GKN Defence Holdings Limited	100	Ordinary
GKN Defence Limited	100	Ordinary
GKN Enterprise Limited	100	Ordinary
GKN Euro Investments Limited	100	Ordinary
GKN Export Services Limited	100	Ordinary
GKN Fasteners Limited	100	Ordinary
GKN Finance (UK) Limited	100	Ordinary
GKN Firth Cleveland Limited	100	Ordinary
GKN Group Pension Trustee (No.2) Limited	100	Ordinary
GKN Group Pension Trustee Limited	100	Ordinary
GKN Group Services Limited	100	Ordinary and redeemable preference
GKN Hardy Spicer Limited	100	Ordinary
GKN Holdings Limited	100	Ordinary
G.K.N. Industries Limited	100	Ordinary
G.K.N. International Trading (Holdings) Limited	100	Ordinary
GKN Limited	100	Ordinary
GKN Marks Limited	100	Ordinary
GKN Overseas Holdings Limited	100	Ordinary
GKN Pistons Limited	100	Ordinary
G.K.N. Powder Met. Limited	100	Ordinary
GKN Quest Trustee Limited	100	Ordinary
GKN Sankey Finance Limited	100	Ordinary and deferred
GKN SEK Investments Limited	100	Ordinary
GKN Service UK Limited	100	Ordinary
GKN Sheepbridge Limited	100	Ordinary
GKN Sheepbridge Stokes Limited	100	Ordinary
GKN Sinter Metals Limited	100	Ordinary
GKN Technology Limited	100	Ordinary
GKN Trading Limited	100	Ordinary
GKN UK Investments Limited	100	Ordinary
GKN U.S. Investments Limited	100	Ordinary
GKN USD Investments Limited	100	Ordinary
GKN Ventures Limited	100	Ordinary
GKN Westland Aerospace (Avonmouth) Limited	100	Ordinary

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
GKN Westland Aerospace Advanced Materials Limited	100	Ordinary and convertible preference
GKN Westland Aerospace Aviation Support Limited	100	Ordinary
GKN Westland Aerospace Holdings Limited	100	Ordinary
GKN Westland Design Services Limited	100	Ordinary
GKN Westland Limited	100	Ordinary
GKN Westland Overseas Holdings Limited	100	Ordinary
GKN Westland Services Limited	100	Ordinary
GKN 1 Trustee 2018 Limited	100	Ordinary
GKN 2 Trustee 2018 Limited	100	Ordinary
GKN 3 Trustee 2018 Limited	100	Ordinary
GKN 4 Trustee 2018 Limited	100	Ordinary
Guest, Keen and Nettlefolds, Limited	100	Ordinary
Harrington Generators International Limited	100	Ordinary
Hawker Siddeley Switchgear Limited	100	Ordinary
Laycock Engineering Limited	100	Ordinary
McKechnie 2005 Pension Scheme Trustee Limited	100	Ordinary
Melrose Holdings Limited	100	Ordinary
Melrose Intermediate Limited	100	Ordinary
Melrose PLC	100	Ordinary
Melrose USD 1 Limited	100	Ordinary
Nevada UK Holding Limited	100	Ordinary
Nortek (UK) Limited	100	Ordinary
Nortek Global HVAC (UK) Limited	100	Ordinary
P.F.D. Limited	100	Ordinary
Raingear Limited	100	Ordinary
Rzeppa Limited	100	Ordinary and redeemable preference
Rigby Metal Components Limited	100	Ordinary
Sageford UK Limited	100	Ordinary
Sheepbridge Stokes Limited	100	Ordinary
Westland Group PLC	100	Ordinary
Westland Group Services Limited	100	Ordinary
Westland System Assessment Limited	100	Ordinary
Whipp & Bourne Limited	100	Ordinary
15 Atholl Crescent, Edinburgh, Scotland, EH3 8HA		
A. P. Newall & Company Limited	100	Ordinary
GKN Investments II GP Limited	100	Ordinary
GKN Investments II LP	100	Membership interest
GKN Investments III GP Limited	100	Ordinary
GKN Investments III LP	100	Membership interest
Chester Road, Erdington, Birmingham, B24 0RB		
GKN Driveline Birmingham Limited	100	Ordinary
Unit 5, Kingsbury Business Park, Kingsbury Road, Minworth, Sutton Coldfield, B76 9DL		
GKN Driveline Service Limited	100	Ordinary
30 Milbank, London, SW1P 4WY		
Hadfields Holdings Limited	37.5	Ordinary
2nd Floor, One Central Boulevard Blythe Valley Park, Shirley, Solihull, B90 8BG		
GKN Aerospace Civil Services Holdings Limited	100	Ordinary
GKN Aerospace Civil Services Limited	100	Ordinary
GKN Aerospace Services Limited	100	Ordinary
2100 The Crescent, Birmingham Business Park, Birmingham, West Midlands, B37 7YE		
GKN Automotive Limited	100	Ordinary and preference
GKN Driveline UK Limited	100	Ordinary
GKN Driveline Mexico (UK) Limited	100	Ordinary
GKN EVO eDrive Systems Limited	100	Ordinary
GKN Freight Services Limited	100	Ordinary and cumulative preference
GKN Hybrid Power Limited	100	Ordinary
Unit 7 Chestnut Court, Jill Lane, Sambourne, Redditch, B96 6EW		
GKN Powder Metallurgy Holdings Limited	100	Ordinary
Unit 1, Cobnar Wood Close, Chesterfield Trading Estate, Chesterfield, Derbyshire, S41 9RQ		
GKN Cylinder Liners UK Limited	100	Ordinary
Uruguay		
Arq. Baldomiro, 2408, Montevideo		
GKN Driveline Uruguay SA *(in liquidation)*	100	Ordinary

Notes to the Company Balance Sheet
Continued

3. Investment in subsidiaries continued

	Equity interest %	Class of Share held
USA		
601 Braddock Avenue, Turtle Creek, Pittsburgh, Pennsylvania, 15145		
Brush Aftermarket North America Inc.	100	Common stock
Generator and Motor Services of Pennsylvania, LLC	100	Membership interest
40 Technology Parkway, South #300, Norcross, GA, 30092		
Aerotron AirPower, Inc.	100	Common stock
Fokker Elmo Inc.	100	Common stock
2345 Rice Street, Suite 230, Roseville MN, 55113		
Ergotron, Inc.	100	Common
1209 Orange Street, Wilmington, Delaware, 19801		
Melrose North America, Inc.	100	Common
PW1100G-JM Engine Leasing, LLC	4	Class C Unit
BBVA Tower 254 Munoz, Rivera Ave, 6th Floor, San Juan, 00918, Puerto Rico		
Nortek Global HVAC de Puerto Rico, LLC	100	Membership interest
601 Abbott Road, Ingham, East Lansing, Michigan, 48823		
Operator Specialty Company, Inc.	100	Common
300 Deschutes Way SW, Suite 304, Tumwater, WA, 98501		
Fokker Aerostructures Inc.	100	Common stock
2710 Gateway Oaks Drive, Suite 150 N, Sacramento, CA, 95833		
GENIL, Inc.	100	Ordinary
GKN Aerospace Camarillo, Inc.	100	Ordinary
GKN Aerospace Chem-tronics Inc.	100	Ordinary
GKN Aerospace Transparency Systems, Inc	100	Common
Nortek Security & Control LLC	100	Membership interest
Zephyr Ventilation, LLC	100	Membership interest
Product Slingshot, Inc.	100	Common stock
251 Little Falls Drive, Wilmington Delaware, 19808		
BNSS LP, Inc.	100	Common
Broan-NuTone LLC	100	Membership interest
GKN Driveline Newton LLC	100	Membership interest
GKN Sinter Metals, LLC	100	Membership interest
GKN Aerospace Aerostructures, Inc	100	Common
GKN Aerospace Florida LLC	100	Membership interest
GKN Aerospace, Inc.	100	Common stock
GKN Aerospace New England, Inc.	100	Ordinary
GKN Aerospace Newington LLC	100	Membership interest
GKN Aerospace St. Louis LLC	100	Membership interest
GKN Aerospace Precision Machining, Inc.	100	Ordinary
GKN Aerospace Services Structures LLC	100	Membership interest
GKN Aerospace South Carolina, Inc.	100	Common stock
GKN Aerospace US Holdings LLC	100	Membership interest
GKN America Corp.	100	Common stock
GKN Cylinder Liners, LLC	100	Membership interest
GKN Driveline North America, Inc.	100	Common stock
GKN Freight Services, Inc.	100	Common stock
GKN North America Investments, Inc.	100	Ordinary
GKN North America Services, Inc.	100	Common
GKN Westland Aerospace, Inc.	100	Common stock
Hoeganaes Corporation	100	Common stock
Huntair Middle East Holdings, Inc.	100	Common
Hoeganaes Specialty Metal Powders LLC	70	Membership interest
IntelliVision Technologies Corp.	100	Ordinary
Nevada Holdco Corp.	100	Ordinary
Nortek Air Solutions, LLC	100	Membership interest
Nortek Global HVAC, LLC	100	Membership interest
Nortek Global HVAC Latin America, Inc.	100	Common
Nortek Home Control Holdings LLC	100	Membership interest
Nortek, Inc.	100	Ordinary
Nortek International, Inc	100	Common
XIK, LLC	100	Membership interest
50 West Broad Street, Suite 1330, Columbus, Ohio, 43215		
GKN Driveline Bowling Green, Inc.	100	Common stock
80 State Street, Albany New York, 12207		
GKN Aerospace Monitor, Inc.	100	Common
135 North Pennsylvania Street, Suite 1610, Indianapolis, Indiana, 46204		
GKN Aerospace Muncie, Inc.	100	Common

Each of the subsidiaries and significant holdings listed are included in the Consolidated Financial Statements of the Company and are held in each case by a subsidiary undertaking, except for Melrose Holdings Limited and GKN Limited, which are held directly by Melrose Industries PLC.

Notes
(1) The Group owns 100% of the Ordinary Class B shares with a total effective ownership of 49% in the company.
(2) The Group owns 9% directly with a total effective ownership of 34.5% in the company.
(3) The Group owns 100% of the Ordinary Class A shares with a total effective ownership of 26% in the company.
(4) The Group owns 49% directly with a total effective ownership of 49.98% in the company.

4. Debtors

	31 December 2020 £m	31 December 2019 £m
Amounts falling due within one year:		
Amounts owed by Group undertakings	**425**	413
Amounts falling due after one year:		
Deferred tax	**29**	25
	454	438

Amounts owed by Group undertakings are either interest-bearing or non interest-bearing depending on the type and duration of the receivable relationship.

The Directors consider that amounts owed by Group undertakings approximate to their fair value.

The deferred tax included in the Balance Sheet is as follows:

	31 December 2020 £m	31 December 2019 £m
Tax losses available for carry forward	**29**	25

The tax losses may be carried forward indefinitely.

5. Creditors

	31 December 2020 £m	31 December 2019 £m
Amounts falling due within one year:		
Amounts owed to Group undertakings	**2,041**	2,015
Accruals and other creditors	**–**	1
	2,041	2,016

Amounts owed to Group undertakings are repayable on demand and are either interest-bearing or non interest-bearing depending on the type and duration of the payable relationship.

The Directors consider that amounts owed to Group undertakings approximate to their fair value.

6. Provisions

	Incentive plan related £m
At 1 January 2020	3
Net credit to profit and loss account	(2)
At 31 December 2020	**1**

The provision for incentive plan related costs relates to employer national insurance costs which are expected to be incurred when the 2020 Employee Share Plan matures. Further details of this plan are set out in the Directors' Remuneration Report. The costs are expected to be incurred within three years.

7. Issued share capital

Share Capital	31 December 2020 £m	31 December 2019 £m
Allotted, called-up and fully paid		
4,858,254,963 (31 December 2019: 4,858,254,963) Ordinary Shares of 48/7 pence each (31 December 2019: 48/7 pence each)	**333**	333
12,831 (31 December 2019: 12,831) 2017 Incentive Plan Shares of £1 each[1]	**–**	–
	333	333

(1) Following the crystallisation of the 2017 Incentive Plan on 31 May 2020 for £nil, the 2017 Incentive Plan shares will be re-designated as deferred shares and cancelled by the Company.

The rights of each class of share are described in the Directors' Report.

8. Related party transactions

The Company has taken the exemption in FRS 102.33: "Related party information" not to disclose intercompany balances and transactions in the year with fully owned subsidiary undertakings.

Glossary

Alternative Performance Measures ("APMs")

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

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

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

Income Statement Measures

APM
Adjusted revenue

Closest equivalent statutory measure
Revenue

Reconciling items to statutory measure
Share of revenue of equity accounted investments (note 5)

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

Revenue	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Revenue	8,770	10,967
Share of revenue of equity accounted investments (note 5)	591	625
Adjusted revenue	**9,361**	11,592

APM
Adjusting items

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Adjusting items (note 6)

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

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

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

APM
Adjusted operating profit

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

Reconciling items to statutory measure
Adjusting items (note 6)

Definition and purpose
The Group uses adjusted profit measures to provide a useful and more comparable measure of the ongoing performance of the Group. Adjusted measures are reconciled to statutory measures by removing adjusting items, the nature of which are disclosed above and further detailed in note 6.

Operating profit	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Operating (loss)/profit	(338)	318
Adjusting items to operating (loss)/profit (note 6)	678	784
Adjusted operating profit	**340**	1,102

APM
Adjusted operating margin

Closest equivalent statutory measure
Operating margin[2]

Reconciling items to statutory measure
Share of revenue of equity accounted investments (note 5) and adjusting items (note 6).

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

APM
Adjusted profit before tax

Closest equivalent statutory measure
(Loss)/profit before tax

Reconciling items to statutory measure
Adjusting items (note 6)

Definition and purpose
Profit before the impact of adjusting items and tax. As discussed above, adjusted profit measures are used to provide a useful and more comparable measure of the ongoing performance of the Group. Adjusted measures are reconciled to statutory measures by removing adjusting items, the nature of which are disclosed above and further detailed in note 6.

Profit before tax	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
(Loss)/profit before tax	(535)	106
Adjusting items to (loss)/profit before tax (note 6)	688	783
Adjusted profit before tax	**153**	889

APM
Adjusted profit after tax

Closest equivalent statutory measure
(Loss)/profit after tax

Reconciling items to statutory measure
Adjusting items (note 6)

Definition and purpose
Profit after tax but before the impact of the adjusting items. As discussed above, adjusted profit measures are used to provide a useful and more comparable measure of the ongoing performance of the Group. Adjusted measures are reconciled to statutory measures by removing adjusting items, the nature of which are disclosed above and further detailed in note 6.

Profit after tax	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
(Loss)/profit after tax	(523)	55
Adjusting items to (loss)/profit after tax (note 6)	643	644
Adjusted profit after tax	**120**	699

APM
Adjusted EBITDA for leverage covenant purposes

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

Reconciling items to statutory measure
Adjusting items (note 6), depreciation of property, plant and equipment and amortisation of computer software and development costs, imputed lease charge, share of non-controlling interests and other adjustments required for covenant purposes[3]

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

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

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

APM
H2 annualised adjusted EBITDA for proforma leverage

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

Reconciling items to statutory measure
Adjusting items (note 6), depreciation of property, plant and equipment and amortisation of computer software and development costs, imputed lease charge, share of non-controlling interests and other adjustments required for covenant purposes[3]

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

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

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

APM
Adjusted tax rate

Closest equivalent statutory measure
Effective tax rate

Reconciling items to statutory measure
Adjusting items, adjusting tax items and the tax impact of adjusting items (note 6 and note 8)

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

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

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

APM
Adjusted basic earnings per share

Closest equivalent statutory measure
Basic earnings per share

Reconciling items to statutory measure
Adjusting items (note 6 and note 10)

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

APM
Adjusted diluted earnings per share

Closest equivalent statutory measure
Diluted earnings per share

Reconciling items to statutory measure
Adjusting items (note 6 and note 10)

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

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

APM
Interest cover

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Not applicable

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

This measure is used for bank covenant testing.

Interest cover	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Adjusted EBITDA for leverage covenant purposes	724	1,505
Adjusted EBITDA from businesses disposed in the year	2	36
Adjusted EBITDA for interest cover	**726**	1,541
Interest on bank loans and overdrafts (note 7)	(136)	(152)
Finance income (note 7)	3	9
Other interest for covenant purposes[4]	(9)	–
Net finance charges for covenant purposes	**(142)**	(143)
Interest cover	**5.1x**	10.8x

Melrose Industries PLC Annual Report 2020

Balance Sheet Measures

APM
Working capital

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

Reconciling items to statutory measure
Not applicable

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

APM
Net debt

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

Reconciling items to statutory measure
Reconciliation of net debt (note 27)

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

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

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

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

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

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

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

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

Net debt	31 December 2020 £m	31 December 2019 £m
Net debt at closing rates (note 27)	2,847	3,283
Impact of foreign exchange	106	94
Net debt at average rates	**2,953**	3,377
Other adjustments required for covenant purposes	–	8
Bank covenant definition of net debt at average rates	**2,953**	3,385
Leverage	**4.1x**	2.25x

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

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

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

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

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

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

Net debt	31 December 2020 £m
Net debt at closing rates (note 27)	2,847
Impact of foreign exchange	85
Net debt at H2 average rates	**2,932**
H2 annualised proforma leverage	**3.2x**

Cash Flow Measures

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

Closest equivalent statutory measure
Net cash from operating activities

Reconciling items to statutory measure
Non-working capital items (note 27)

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

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

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

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

APM
Movement in net working capital and percentage change

Closest equivalent statutory measure
Change in inventories, change in receivables and change in payables as included within net cash from operating activities (note 27)

Reconciling items to statutory measure
Not applicable

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

Movement in working capital	Year ended 31 December 2020 £m	Year ended 31 December 2019 £m
Change in inventories (note 27)	187	(12)
Change in receivables (note 27)	250	72
Change in payables (note 27)	(13)	(2)
Movement in working capital	**424**	58
	Year ended 31 December 2019 £m	**Year ended 31 December 2018 £m**
Net working capital comprises:		
Inventories (note 16)	1,332	1,489
Current trade and other receivables (note 17)	1,970	2,328
Non-current trade and other receivables (note 17)	424	504
Current trade and other payables (note 19)	(2,461)	(2,583)
Non-current trade and other payables (note 19)	(444)	(762)
Net working capital	**821**	976
Percentage reduction in net working capital	**52%**	6%

APM
Free cash flow

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

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

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

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

APM
Adjusted free cash flow

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

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

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

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

APM
Capital expenditure (capex)

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Not applicable

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

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

APM
Capital expenditure to depreciation ratio

Closest equivalent statutory measure
None

Reconciling items to statutory measure
Not applicable

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

APM
Dividend per share

Closest equivalent statutory measure
Dividend per share

Reconciling items to statutory measure
Not applicable

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

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

Notice of Annual General Meeting

The Annual General Meeting of Melrose Industries PLC (the "Company") will be held at 11.00 a.m. on Thursday 6 May 2021 at Leconfield House, Curzon Street, London W1J 5JA.

This document is important and requires your immediate attention. If you are in any doubt as to the action you should take, you should consult your stockbroker, bank, solicitor, accountant, fund manager or other independent financial adviser authorised under the Financial Services and Markets Act 2000 if you are resident in the United Kingdom or, if not, another appropriately authorised independent financial adviser.

COVID-19 and contingencies

Our preference had been to welcome shareholders in person to our 2021 Annual General Meeting, particularly given the constraints we faced in 2020 due to the COVID-19 pandemic. However, at the time of publication of this notice, national lockdown restrictions would not allow shareholders to attend the Annual General Meeting in person. We are therefore proposing to hold the Annual General Meeting at the Company's offices at Leconfield House, Curzon Street, London W1J 5JA with the minimum attendance required to form a quorum. Shareholders will not be permitted to attend the Annual General Meeting in person, but can be represented by the Chairman of the Annual General Meeting acting as their proxy (as detailed in the explanatory notes starting on page 211).

Given the constantly evolving nature of the situation, should circumstances change before the time of the Annual General Meeting, we want to ensure that we are able to adapt arrangements and to welcome shareholders to the Annual General Meeting, within safety constraints and in accordance with government guidelines. Should we consider that it has become possible to do so, we will notify shareholders of any change to our meeting arrangements as early as is possible before the date of the meeting, by publishing details of the changes on our website at **www.melroseplc.net**, and, if practicable, by issuing a further communication via a regulatory news service and publishing a notice of the change in two national daily newspapers.

Given the uncertainty around whether shareholders will be able to attend the Annual General Meeting, we recommend that all shareholders complete and return a form of proxy, appointing the Chairman of the Annual General Meeting as their proxy. This will ensure that your vote will be counted even if attendance at the meeting is restricted or you are unable to attend in person. Please see the explanatory notes starting on page 211 for guidance on how to complete your proxy form and by when.

Notice of Annual General Meeting

If you have sold or otherwise transferred or sell or otherwise transfer all of your shares in the Company, please send this document, together with the accompanying form of proxy, as soon as possible to the purchaser or transferee or to the agent through whom the sale or transfer was effected for delivery to the purchaser or transferee.

Notice is given that the Annual General Meeting of the Company will be held at Leconfield House, Curzon Street, London W1J 5JA at 11.00 a.m. on Thursday 6 May 2021 for the purposes set out below. Resolutions 1 to 17 (inclusive) will be proposed as ordinary resolutions and resolutions 18 to 21 (inclusive) as special resolutions.

Ordinary resolutions

1. To receive the Company's audited financial statements for the financial year ended 31 December 2020, together with the Directors' Report, the Strategic Report and the Auditor's Report on those financial statements.
2. To approve the Directors' Remuneration Report for the year ended 31 December 2020, as set out on pages 110 to 126 of the Company's 2020 Annual Report.
3. To declare a final dividend of 0.75 pence per ordinary share for the year ended 31 December 2020.
4. To re-elect Christopher Miller as a Director of the Company.
5. To re-elect David Roper as a Director of the Company.
6. To re-elect Simon Peckham as a Director of the Company.
7. To re-elect Geoffrey Martin as a Director of the Company.
8. To re-elect Justin Dowley as a Director of the Company.
9. To re-elect Liz Hewitt as a Director of the Company.
10. To re-elect David Lis as a Director of the Company.
11. To re-elect Archie G. Kane as a Director of the Company.
12. To re-elect Charlotte Twyning as a Director of the Company.
13. To re-elect Funmi Adegoke as a Director of the Company.
14. To elect Peter Dilnot as a Director of the Company.
15. To re-appoint Deloitte LLP as auditor of the Company to hold office from the conclusion of this meeting until the conclusion of the next Annual General Meeting of the Company at which accounts are laid.
16. To authorise the Audit Committee to determine the remuneration of the auditor of the Company.
17. That, in accordance with section 551 of the Companies Act 2006 (the "Act"), the directors of the Company (the "Directors") be and are generally and unconditionally authorised to allot shares in the Company, or to grant rights to subscribe for or to convert any security into shares in the Company ("Rights"):

    (A) up to an aggregate nominal amount of £111,045,827; and

    (B) comprising equity securities (as defined in section 560 of the Act) up to an aggregate nominal amount of £222,091,655 (such amount to be reduced by the aggregate nominal amount of any allotments or grants made under paragraph (A) of this resolution) in connection with an offer by way of a rights issue:

    (i) to ordinary shareholders in proportion (as nearly as may be practicable) to their existing holdings; and

    (ii) to holders of other equity securities as required by the rights of those securities or, subject to such rights, as the Directors otherwise consider necessary,

    and so that the Directors may impose any limits or restrictions and make any arrangements which they consider necessary or appropriate to deal with treasury shares, fractional entitlements, record dates, legal, regulatory or practical problems in, or under the laws of any territory or any other matter, such authorities to expire at the conclusion of the Company's next Annual General Meeting after this resolution is passed or, if earlier, at the close of business on 30 June 2022, but, in each case, so that the Company may make offers or agreements before the authority expires which would or might require shares to be allotted or Rights to be granted after the authority expires, and so that the Directors may allot shares or grant Rights in pursuance of any such offer or agreement notwithstanding that the authority conferred by this resolution has expired.

Special resolutions

18. That, subject to the passing of resolution 17, the Directors be and are generally empowered to allot equity securities (as defined in section 560 of the Act) for cash pursuant to the authorities granted by resolution 17 and/or to sell ordinary shares held by the Company as treasury shares for cash, in each case as if section 561 of the Act did not apply to any such allotment or sale, provided that this power shall be limited:

    (A) to the allotment of equity securities in connection with an offer of equity securities (but in the case of an allotment pursuant to the authority granted under paragraph (B) of resolution 17, such power shall be limited to the allotment of equity securities in connection with an offer by way of a rights issue only):

    (i) to ordinary shareholders in proportion (as nearly as may be practicable) to their existing holdings; and

    (ii) to holders of other equity securities, as required by the rights of those securities or, subject to such rights, as the Directors otherwise consider necessary, and so that the Directors may impose any limits or restrictions and make any arrangements which they consider necessary or appropriate to deal with treasury shares, fractional entitlements, record dates, legal, regulatory or practical problems in, or under the laws of, any territory or any other matter; and

    (B) to the allotment (otherwise than in circumstances set out in paragraph (A) of this resolution) of equity securities pursuant to the authority granted by paragraph (A) of resolution 17 or sale of treasury shares up to a nominal amount of £16,656,874,

    such powers to expire at the conclusion of the Company's next Annual General Meeting after this resolution is passed or, if earlier, at the close of business on 30 June 2022, but, in each case, so that the Company may make offers or agreements before the power expires which would or might require equity securities to be allotted (and/or treasury shares sold) after the power expires and so that the Directors may allot equity securities (and/or sell treasury shares) in pursuance of any such offer or agreement notwithstanding that the power conferred by this authority has expired.
19. That, subject to the passing of resolution 17 and in addition to any power granted under resolution 18, the Directors be and are generally empowered to allot equity securities (as defined in section 560 of the Act) for cash pursuant to the authorities granted by resolution 17 and/or to sell ordinary shares held by the Company as treasury shares for cash, in each case as if section 561 of the Act did not apply to any such allotment or sale, provided that this power shall be:

    (A) limited to the allotment of equity securities pursuant to the authority granted by paragraph (A) of resolution 17 or sale of treasury shares up to a nominal amount of £16,656,874; and

    (B) used only for the purposes of financing (or refinancing, if the authority is to be used within six months of the original transaction) a transaction which the Directors determine to be an acquisition or other capital investment of a kind contemplated by the Statement of Principles on Disapplying Pre-Emption Rights most recently published by the Pre-Emption Group prior to the date of this notice of the Annual General Meeting,

    such powers to expire at the conclusion of the Company's next Annual General Meeting after this resolution is passed or, if earlier, at the close of business on 30 June 2022, but, in each case, so that the Company may make offers or agreements before the power expires which would or might require equity securities to be allotted (and/or treasury shares sold) after the power expires and so that the Directors may allot equity securities (and/or sell treasury shares) in pursuance of any such offer or agreement notwithstanding that the power conferred by this authority has expired.
20. That the Company be and is generally and unconditionally authorised to make one or more market purchases (within the meaning of section 693 of the Act) of ordinary shares in the capital of the Company provided that:

    (A) the maximum aggregate number of ordinary shares authorised to be purchased is 485,825,496;

    (B) the minimum price which may be paid for an ordinary share is the nominal value of an ordinary share at the time of such purchase;

    (C) the maximum price which may be paid for an ordinary share is not more than the higher of:

    (i) 105% of the average of the middle-market quotation for an ordinary share as derived from the Daily Official List of the London Stock Exchange for the five business days immediately preceding the day on which the ordinary share is purchased; and

    (ii) the higher of the price of the last independent trade and the highest current independent bid on the trading venue where the purchase is carried out, in each case, exclusive of expenses;

    (D) this authority shall expire at the conclusion of the Company's next Annual General Meeting after this resolution is passed or, if earlier, at the close of business on 30 June 2022;

    (E) the Company may make a contract of purchase of ordinary shares under this authority which would or might be executed wholly or partly after the expiry of this authority, and may make a purchase of ordinary shares in pursuance of any such contract; and

    (F) any ordinary shares purchased pursuant to this authority may either be held as treasury shares or cancelled by the Company, depending on which course of action is considered by the Directors to be in the best interests of shareholders at the time.
21. That a general meeting other than an Annual General Meeting may be called on not less than 14 clear days' notice.

Recommendation

The Board believes that each of the resolutions to be proposed at the Annual General Meeting is in the best interests of the Company and its shareholders as a whole. Accordingly, the Directors unanimously recommend that ordinary shareholders vote in favour of all of the resolutions proposed, as the Directors intend to do in respect of their own beneficial holdings.

By order of the Board

Jonathon Crawford
Company Secretary
31 March 2021

Registered Office:
11th Floor The Colmore Building
20 Colmore Circus Queensway
Birmingham
West Midlands
B4 6AT

Melrose Industries PLC Annual Report 2020

Notice of Annual General Meeting

Continued

Explanatory notes to the proposed resolutions

Resolutions 1 to 17 (inclusive) are proposed as ordinary resolutions, which means that for each of those resolutions to be passed, more than half the votes cast must be cast in favour of the resolution. Resolutions 18 to 21 (inclusive) are proposed as special resolutions, which means that for each of those resolutions to be passed, at least three-quarters of the votes cast must be cast in favour of the resolution.

Resolution 1 – Receipt of 2020 Annual Report and Financial Statements

The Directors are required to lay the Company's financial statements, the Strategic Report and the Directors' and auditor's reports on those financial statements (collectively, the "2020 Annual Report") before shareholders each year at the Annual General Meeting ("AGM").

Resolution 2 – Approval of Directors' remuneration report

The Directors' remuneration report (the "Directors' Remuneration Report") is presented in two sections:

- the annual statement from the Chairman of the Remuneration Committee; and
- the annual report on remuneration.

The annual statement from the Chairman of the Remuneration Committee, set out on pages 110 to 111 of the 2020 Annual Report, summarises, for the year ended 31 December 2020, the major decisions taken on Directors' remuneration, any substantial changes relating to Directors' remuneration made during the year and the context in which those changes occurred and decisions that have been taken.

The annual report on remuneration, set out on pages 112 to 126 of the 2020 Annual Report, provides details of the remuneration paid to Directors in respect of the year ended 31 December 2020, including base salary, taxable benefits, short-term incentives, long-term incentives vested in the year, pension-related benefits, any other items in the nature of remuneration and any sum(s) recovered or withheld during the year in respect of amounts paid in earlier years.

The Directors' Remuneration Report is subject to an annual advisory shareholder vote by way of an ordinary resolution. Resolution 2 is to approve the Directors' Remuneration Report.

Resolution 3 – Declaration of final dividend

The Board is recommending, and shareholders are being asked to approve, the declaration of a final dividend of 0.75p per ordinary share for the year ended 31 December 2020. The final dividend will, subject to shareholder approval, be paid on 19 May 2021 to the holders of ordinary shares whose names are recorded on the register of members of the Company at the close of business on 6 April 2021.

Resolutions 4 to 13 (inclusive) – Re-election of Directors

In accordance with the UK Corporate Governance Code (the "Code") and the Company's Articles of Association (the "Articles"), every Director will stand for re-election at the AGM, with the exception of Peter Dilnot, who is standing for election.

The Board considers that the contribution of each Director who is standing for re-election is, and continues to be, important to the sustainable success of the Company for the following reasons:

- Justin Dowley, Non-executive Chairman, is standing for re-election as Director due to his extensive and long-standing experience within the banking, investment and asset management sectors. Mr Dowley first joined the Board as a Non-executive Director in September 2011 and served as Senior Independent Director in the two years prior to his appointment as Non-executive Chairman, meaning he has served for just over nine years. Given the global pandemic, the acquisition of GKN, and the elevation of the Company to the FTSE 100, the Nomination Committee and Board consider that there is a need for continuity and stability at Board level to facilitate succession planning arrangements and the development of a diverse Board. Mr Dowley was considered independent upon his appointment as Non-executive Chairman.
- Simon Peckham, Chief Executive, is standing for re-election as Director due to his deep understanding of the Melrose business model, having joined the Company initially in 2003 as Chief Operating Officer. He has widespread expertise in corporate finance, mergers and acquisitions, strategy and operations.
- Christopher Miller, Vice-Chairman, is standing for re-election on the basis of his deep understanding of the Melrose business model, having co-founded Melrose. Mr Miller has long-standing involvement in manufacturing industries and private investment.
- David Roper, Vice-Chairman, is standing for re-election on the basis of his deep understanding of the Melrose business model, having co-founded Melrose. Mr Roper has longstanding involvement in corporate finance, private investment and management in manufacturing industries. Mr Roper will be retiring from the Board on 31 May 2021.
- Geoffrey Martin, Group Finance Director, is standing for re-election due to his deep understanding of the Melrose business model, having been appointed as Group Finance Director in 2005. He also brings to the Board considerable public company experience and expertise in corporate finance, equity finance raising and financial strategy.
- Liz Hewitt, Senior Independent Director, is standing for re-election as Director due to her extensive business, financial and investment experience gained from a number of senior roles in international companies. In particular, Ms Hewitt is the longest serving Non-executive Director after the Chairman, having served on the Board since 2013, and fulfils the pre-requisite of being independent.
- David Lis, Non-executive Director, is standing for re-election due to his extensive financial experience and deep insight into the expectations of Melrose's institutional investor base, having held several roles in investment management.
- Archie G. Kane, Non-executive Director, is standing for re-election due to his extensive financial and general management expertise, having held several roles in the financial services sector and public company boards.
- Charlotte Twyning, Non-executive Director, is standing for re-election due to her diverse range of experience and commercial acumen having held various senior positions in the telecommunications and transport sectors, and most recently in aviation.
- Funmi Adegoke, Non-executive Director, is standing for re-election due to her diverse industrial knowledge as well as significant transactional and commercial management expertise based on her extensive experience working in and leading legal teams across the globe at multi-national organisations.

Biographical details of each Director can be found on pages 92 to 93 of the 2020 Annual Report. All of the Non-executive Directors standing for re-election are currently considered independent under the Code.

Resolution 14 – Election of Director

In accordance with the Articles, Peter Dilnot, Chief Operating Officer, is standing for election as a Director of the Company following his appointment to the Board with effect from 1 January 2021. Mr Dilnot brings to the Board a deep understanding of the Melrose business model together with strong sector experience in engineering and aviation.

Biographical details for Peter Dilnot can be found on page 93 of the 2020 Annual Report.

Resolution 15 – Re-appointment of auditor

The Company is required to appoint auditors at each general meeting at which accounts are laid before shareholders, to hold office until the next such meeting.

The Audit Committee has reviewed the effectiveness, performance, independence and objectivity of the existing external auditor, Deloitte LLP, on behalf of the Board, and concluded that the external auditor was in all respects effective.

This resolution proposes the re-appointment of Deloitte LLP until the conclusion of the next AGM.

Resolution 16 – Authority to agree auditor's remuneration

This resolution seeks authority for the Audit Committee to determine the level of the auditor's remuneration.

Resolution 17 – Authority to allot shares

This resolution seeks shareholder approval to grant the Directors the authority to allot shares in the Company, or to grant rights to subscribe for or convert any securities into shares in the Company ("Rights"), pursuant to section 551 of the Act (the "Section 551 authority"). The authority contained in paragraph (A) of the resolution will be limited to an aggregate nominal amount of £111,045,827, being approximately one-third of the Company's issued ordinary share capital as at 30 March 2021 (being the last business day prior to the publication of this notice).

In line with guidance issued by the Investment Association, paragraph (B) of this resolution would give the Directors authority to allot shares in the Company or grant Rights in connection with a rights issue up to aggregate nominal amount of £222,091,655, representing approximately two-thirds of the Company's issued ordinary share capital as at 30 March 2021. This resolution provides that such amount shall be reduced by the aggregate nominal amount of any allotments or grants under paragraph (A).

The Company does not hold any shares in treasury.

If approved, the Section 551 authority shall, unless renewed, revoked or varied by the Company, expire at the end of the Company's next AGM after the resolution is passed or, if earlier, at the close of business on 30 June 2022. The exception to this is that the Directors may allot shares or grant Rights after the authority has expired in connection with an offer or agreement made or entered into before the authority expired. The Directors have no present intention to exercise the Section 551 authority.

Resolutions 18 to 19 – Partial disapplication of pre-emption rights

These resolutions seek shareholder approval to grant the Directors the power to allot equity securities (as defined by section 560 of the Act) or sell treasury shares of the Company pursuant to sections 570 and 573 of the Act (the "Section 570 and 573 power") without first offering them to existing shareholders in proportion to their existing shareholdings.

The power is limited to allotments for cash in connection with pre-emptive offers, subject to any arrangements that the Directors consider appropriate to deal with fractions and overseas requirements and otherwise for cash up to a maximum nominal value of £33,313,748, representing approximately 10% of the Company's issued ordinary share capital as at 30 March 2021 (being the last business day prior to the publication of this notice).

The Directors intend to adhere to the guidelines set out in the Pre-Emption Group's Statement of Principles (as updated in March 2015) and not to allot shares for cash on a non pre-emptive basis pursuant to a relevant authority in resolutions 18 or 19:

- in excess of an amount equal to 5% of the Company's issued ordinary share capital (excluding treasury shares) in any one-year period, whether or not in connection with an acquisition or specified capital investment; or
- in excess of an amount equal to 7.5% of the Company's issued ordinary share capital in a rolling three-year period,

in each case other than in connection with an acquisition or specified capital investment which is announced contemporaneously with the allotment or which has taken place in the preceding six-month period and is disclosed in the announcement of the allotment.

If approved, the Section 570 and 573 power shall apply until the end of the Company's next AGM after the resolutions are passed or, if earlier, until the close of business on 30 June 2022. The exception to this is that the Directors may allot equity securities after the power has expired in connection with an offer or agreement made or entered into before the power expired. The Directors have no present intention to exercise the Section 570 and 573 power.

Resolution 20 – Authority to purchase own shares

This resolution seeks shareholder approval to grant the Company the authority to purchase its own shares pursuant to sections 693 and 701 of the Act.

This authority is limited to an aggregate maximum number of 485,825,496 ordinary shares, representing 10% of the Company's issued ordinary share capital as at 30 March 2021.

The maximum price which may be paid for an ordinary share will be an amount which is not more than the higher of: (i) 5% above the average of the middle market quotation for an ordinary share as derived from the Daily Official List of the London Stock Exchange for the five business days immediately preceding the day on which the ordinary share is purchased; and (ii) the higher of the price of the last independent trade and the highest current independent bid on the trading venue where the purchase is carried out (in each case, exclusive of expenses).

If approved, the authority shall, unless varied, revoked or renewed, expire at the end of the Company's next AGM after the resolution is passed or, if earlier, at the close of business on 30 June 2022. The Directors have no present intention of exercising all or any of the powers conferred by this resolution and will only exercise their authority if it is in the interests of shareholders generally.

Resolution 21 – Notice period for general meetings other than AGMs

This resolution seeks shareholder approval to allow the Company to continue to call general meetings (other than AGMs) on 14 clear days' notice. In accordance with the Act, as amended by the Companies (Shareholders' Rights) Regulations 2009, the notice period required for general meetings of the Company is 21 clear days unless shareholders approve a shorter notice period (subject to a minimum period of 14 clear days). In accordance with the Act, the Company must make a means of electronic voting available to all shareholders for that meeting in order to be able to call a general meeting on less than 21 clear days' notice.

The Company intends to only use the shorter notice period where this flexibility is merited by the purpose of the meeting and is considered to be in the interests of shareholders generally, and not as a matter of routine. AGMs will continue to be held on at least 21 clear days' notice.

The approval will be effective until the Company's next AGM, when it is intended that a similar resolution will be proposed.

Explanatory notes as to the proxy, voting and attendance procedures at the Annual General Meeting (AGM)

1. As a result of the current COVID-19 pandemic and the legislative measures and associated guidance introduced by the UK Government in response, we are currently unable to welcome shareholders in person at the AGM, and it is proposed that the AGM will be held as a closed meeting with only director shareholders necessary for a quorum in physical attendance. Attendance by other shareholders at the AGM in person will not be possible and members or their appointed proxies (other than the Chairman of the AGM) will not be permitted entry to the AGM. In the event that our meeting arrangements change subsequent to publication of this Notice of AGM, the Company will publish details on its website at **www.melroseplc.net**, and, if practicable, issue a further communication via a regulatory news service and publish a notice of the change in two national daily newspapers.
2. The holders of ordinary shares in the Company are entitled to vote. A member entitled to vote at the AGM is also entitled to appoint a proxy to exercise all or any of his/her rights to vote at the AGM in his/her place.

Notice of Annual General Meeting

Continued

Explanatory notes as to the proxy, voting and attendance procedures at the Annual General Meeting (AGM) continued

3. Members are entitled to appoint a proxy to vote on their behalf at the AGM. The appointment of a person other than the Chairman of the AGM as your proxy will not be valid, as that person will also not be permitted to attend the meeting in person in order to vote on your behalf. Accordingly, in order to ensure your votes are counted, the Board recommends that members appoint the Chairman of the AGM as their proxy with their voting instructions. A form of proxy which may be used to appoint the Chairman and give proxy instructions for use at the AGM is enclosed with this notice. To be effective, a form of proxy must be completed and returned, together with any power of attorney or authority under which it is completed or a certified copy of such power or authority, so that it is received by the Company's registrars at the address specified on the form of proxy not less than 48 hours (excluding any part of a day that is not a working day) before the stated time for holding the meeting (or, in the event of an adjournment, not less than 48 hours before the stated time of the adjourned meeting (excluding any part of a day which is not a working day)).
4. Any person to whom this notice is sent who is a person nominated under section 146 of the Act to enjoy information rights (a "Nominated Person") may, under an agreement between him/her and the shareholder by whom he/she was nominated, have a right to be appointed (or to have someone else appointed) as a proxy for the AGM. If a Nominated Person has no such proxy appointment right or does not wish to exercise it, he/she may, under any such agreement, have a right to give instructions to the shareholder as to the exercise of voting rights. The statement of the rights of shareholders in relation to the appointment of proxies in paragraphs 2 and 3 on page 212 and above respectively does not apply to Nominated Persons. The rights described in paragraphs 2 and 3 can only be exercised by the holders of ordinary shares in the Company. Notwithstanding any right of the Nominated Person to be appointed as proxy, as stated above, the appointment of a person other than the Chairman of the AGM will be invalid, as that person will not be permitted to attend the meeting in person in order to vote on behalf of the Nominated Person.
5. To be entitled to vote at the AGM (and for the purposes of the determination by the Company of the number of votes they may cast), members must be entered on the Company's register of members by 6.30 p.m. BST on 4 May 2021 (or, in the event of an adjournment, on the date which is two days, excluding any day which is not a working day, before the time of the adjourned meeting). Changes to entries on the register of members after this time shall be disregarded in determining the rights of any person to vote at the meeting.
6. As at 30 March 2021 (being the last business day prior to the publication of this notice), the Company's issued ordinary share capital consists of 4,858,254,963 ordinary shares of 48/7p each, carrying one vote each.
7. CREST members who wish to appoint a proxy or proxies through the CREST electronic proxy appointment service may do so by using the procedures described in the CREST Manual (available at **www.euroclear.com**). CREST Personal Members or other CREST sponsored members, and those CREST members who have appointed a service provider(s), should refer to their CREST sponsor or voting service provider(s), who will be able to take the appropriate action on their behalf.
8. In order for a proxy appointment or instruction made using the CREST service to be valid, the appropriate CREST message (a "CREST Proxy Instruction") must be properly authenticated in accordance with Euroclear UK & Ireland Limited's specifications, and must contain the information required for such instruction, as described in the CREST Manual. The message, regardless of whether it constitutes the appointment of a proxy or is an amendment to the instruction given to a previously appointed proxy, must, in order to be valid, be transmitted so as to be received by the issuer's agent (ID RA19) by 11.00 a.m. (BST) on 4 May 2021. For this purpose, the time of receipt will be taken to be the time (as determined by the time stamp applied to the message by the CREST Application Host) from which the issuer's agent is able to retrieve the message by enquiry to CREST in the manner prescribed by CREST. After this time any change of instructions to proxies appointed through CREST should be communicated to the appointee through other means.
9. CREST members and, where applicable, their CREST sponsors, or voting service providers should note that Euroclear UK & Ireland Limited does not make available special procedures in CREST for any particular message. Normal system timings and limitations will, therefore, apply in relation to the input of CREST Proxy Instructions. It is the responsibility of the CREST member concerned to take (or, if the CREST member is a CREST Personal Member, or sponsored member, or has appointed a voting service provider, to procure that his/ her CREST sponsor or voting service provider(s) take(s)) such action as shall be necessary to ensure that a message is transmitted by means of the CREST system by any particular time. In this connection, CREST members and, where applicable, their CREST sponsors or voting system providers are referred, in particular, to those sections of the CREST Manual concerning practical limitations of the CREST system and timings.
10. The Company may treat as invalid a CREST Proxy Instruction in the circumstances set out in Regulation 35(5) (a) of the Uncertificated Securities Regulations 2001.
11. Any corporation which is a member can appoint one or more corporate representatives who may exercise on its behalf all of its powers as a member provided that they do not do so in relation to the same shares.
12. Under section 527 of the Act, members meeting the threshold requirements set out in that section have the right to require the Company to publish on a website a statement setting out any matter relating to: (i) the audit of the Company's accounts (including the auditor's report and the conduct of the audit) that are to be laid before the AGM; or (ii) any circumstance connected with an auditor of the Company ceasing to hold office since the previous meeting at which annual accounts and reports were laid in accordance with section 437 of the Act. The Company may not require the shareholders requesting any such website publication to pay its expenses in complying with sections 527 or 528 of the Act. Where the Company is required to place a statement on a website under section 527 of the Act, it must forward the statement to the Company's auditor not later than the time when it makes the statement available on the website. The business which may be dealt with at the AGM includes any statement that the Company has been required under section 527 of the Act to publish on a website.
13. The Company will offer an opportunity for members to engage in advance of the meeting through an online facility to submit questions. If members have any questions for the Board in relation to the business being dealt with at the AGM, these can be submitted using the online service that can be accessed from **https://www.melroseplc.net/investors/shareholder-information/melrose-agm-2021-questions-form/**. Questions must be received by no later than 11.00 a.m. (BST) on 4 May 2021. The Board will upload a response to these questions on our website that endeavours to answer the key themes of these questions, but no answer need be given if: (i) to do so would interfere unduly with the preparation for the meeting or involve the disclosure of confidential information; (ii) the answer has already been given on a website in the form of an answer to a question; and/or (iii) it is undesirable in the interests of the Company or the good order of the meeting that the question be answered.

14. Voting at the AGM will be by poll. All valid proxy votes, whether submitted electronically or in hard copy form, will be included in the poll to be taken at the meeting. In addition, the Chairman of the AGM will cast the votes for which he has been appointed as proxy. Once the results have been verified by the Company's registrar, Equiniti, they will be notified to the Financial Conduct Authority, announced through a Regulatory Information Service and will be available to view on the Company's website.
15. A copy of this notice, and other information required by section 311A of the Act, can be found at **www.melroseplc.net**.
16. You may not use an electronic address provided in either this Notice of AGM or any related documents (including the form of proxy) to communicate with the Company for any purposes other than those expressly stated.
17. The following documents will be available for inspection upon request at the Company's registered office during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) from the date of this notice up to and including the date of the AGM and at the place of the AGM for 15 minutes prior to and during the meeting:
    (A) copies of all service agreements under which Directors of the Company are employed by the Company or any subsidiaries; and
    (B) a copy of the terms of appointment of the Non-executive Directors of the Company.
18. You may register your vote online by visiting Equiniti's website at **www.sharevote.co.uk**. In order to register your vote online, you will need to enter the Voting ID, Task ID and Shareholder Reference Number which are set out on the enclosed form of proxy. Shareholders who have already registered with Equiniti's online portfolio service, Shareview, can appoint their proxy electronically by logging on to their portfolio at **www.shareview.co.uk** using your usual user ID and password. Once logged in simply click "View" on the "My Investments" page, click on the link to vote then follow the on-screen instructions. A proxy appointment made electronically will not be valid if sent to any address other than those provided or if received after 11.00 a.m. (BST) on 4 May 2021.

Company and shareholder information

As at 31 December 2020, there were 18,608 holders of ordinary shares of 48/7 pence each in the Company. An analysis of these shareholdings as at 31 December 2020 is set out in the table below.

Shareholder analysis

Balance Ranges	Total number of holdings	Percentage of holders	Total number of shares	Percentage issued capital
1–5,000	14,321	76.96%	18,587,442	0.38%
5,001–50,000	3,356	18.04%	43,496,230	0.90%
50,001–500,000	498	2.68%	88,613,514	1.82%
Over 500,000	433	2.33%	4,707,557,777	96.90%
Total	**18,608**	**100.00%**	**4,858,254,963**	**100.00%**
Held by				
Individuals	15,856	85.21%	55,827,867	1.15%
Institutions	2,752	14.79%	4,802,427,096	98.85%
Total	**18,608**	**100.00%**	**4,858,254,963**	**100.00%**

Financial calendar 2021

Ex-dividend date for final dividend	1 April 2021
Record date for final dividend	6 April 2021
Annual General Meeting	6 May 2021
Payment date of final dividend	19 May 2021
Announcement of interim results	September 2021
Intended payment of interim dividend	October 2021
Preliminary announcement of 2021 results	March 2022

Registrar
Equiniti
Aspect House
Spencer Road
Lancing
West Sussex BN99 6DA

Tel: 0371 384 2030 or +44 (0) 121 415 7047 (from outside UK)

Lines are open from 8.30 am to 5.30 pm Monday to Friday, excluding public holidays in England and Wales.

Brokers
Investec
2 Gresham Street
London EC2V 7QP

J.P. Morgan Cazenove
25 Bank Street
London E14 5JP

Legal Advisers
Simpson Thacher & Bartlett LLP
CityPoint
One Ropemaker Street
London EC2Y 9HU

Bankers
ABN AMRO Bank N.V.
Banca IMI S.p.A, London Branch
Banco Santander S.A., London Branch
Bank of America Merrill Lynch International Limited
Bank of China Limited, London Branch
Barclays Bank plc
Bayerische Landesbank
BNP Paribas Fortis SA/NV
Caixabank SA, UK Branch
Citibank, N.A., London Branch
Citizens Bank, N.A.
Commerzbank Aktiengesellschaft, London Branch
Crédit Agricole Corporate and Investment Bank
Crédit Industriel et Commercial
Deutsche Bank Luxembourg S.A.
HSBC Bank plc
Industrial and Commercial Bank of China Limited, London Branch
ING Bank N.V., London Branch
J.P. Morgan Chase Bank N.A., London Branch
Mediobanca International (Luxembourg) S.A.
National Westminster Bank plc
Royal Bank of Canada
Skandinaviska Enskilda Banken AB (publ)
Standard Chartered Bank
The Governor and Company of the Bank of Ireland
UniCredit Bank AG
Wells Fargo Bank, N.A., London Branch

A range of shareholder information is available at Equiniti's online portfolio service **www.shareview.co.uk**, where you can register for a Shareview Portfolio to access information about your holding and undertake a number of activities, including appointing a proxy, changing a dividend mandate and updating your address. To register, you will need your 11-digit Shareholder Reference Number (SRN), which can be found on your proxy form or dividend voucher.

Gifting your shares
If you have a small number of shares and the dealing costs or minimum fee make it uneconomical to sell them, you may like to donate them to benefit charities through ShareGift, a registered charity. Further information is available on the ShareGift website at **www.sharegift.org** or call +44 (0) 20 7930 3737.

Share fraud warning
Many companies have become aware that their shareholders have received unsolicited telephone calls or correspondence concerning investment matters. Fraudsters use persuasive and high-pressure tactics to lure investors into scams. They may offer to sell shares that turn out to be worthless or non-existent, or to buy shares at an inflated price in return for an upfront payment. For more detailed information on this kind of activity or to report a scam, please call the Financial Conduct Authority's Consumer Helpline on +44 (0)800 111 6768 or visit **www.fca.org.uk/consumers/scams**.

Notes

Notes

Buy
Improve
Sell

Melrose

www.melroseplc.net

London Stock Exchange
Code: MRO
SEDOL: BZ1G432
LEI: 213800RGNXXZY2M7TR85

Melrose Industries PLC

Registered Office
11th Floor, The Colmore Building
20 Colmore Circus Queensway
Birmingham
West Midlands
B4 6AT

Tel: +44 (0) 121 296 2800
Fax: +44 (0) 121 296 2839

Registered Number: 09800044

Head Office
Leconfield House
Curzon Street
London
W1J 5JA

Tel: +44 (0) 20 7647 4500
Fax: +44 (0) 20 7647 4501

North America Office
1180 Peachtree Street NE
Suite 2450
Atlanta
GA 30309

Tel: +1 404 941 2100
Fax: +1 404 941 2772