Chemring Group

Delivering global protection

Chemring Group PLC

Results for the six months to 30 April 2017

Interim FY17 scorecard

Revenue

£249.6m

⇧39%

Significant growth achieved in Energetics segment

Operating profit*

£17.2m

⇧£13.4m

Improvement reflects large contracts in Energetics segment continuing from H2 2016

Order book

£556.2m

⇩6%

Anticipated H2 revenue approximately 85% covered by orders in hand

Progress

Operational momentum of H2 2016 continued and customer deliveries made to plan

Safety

Remains our first priority

FY17 outlook

H2 weighting less pronounced

Full year outlook in line with the Board's expectations

* *References to operating profit and earnings per share are to underlying measures*

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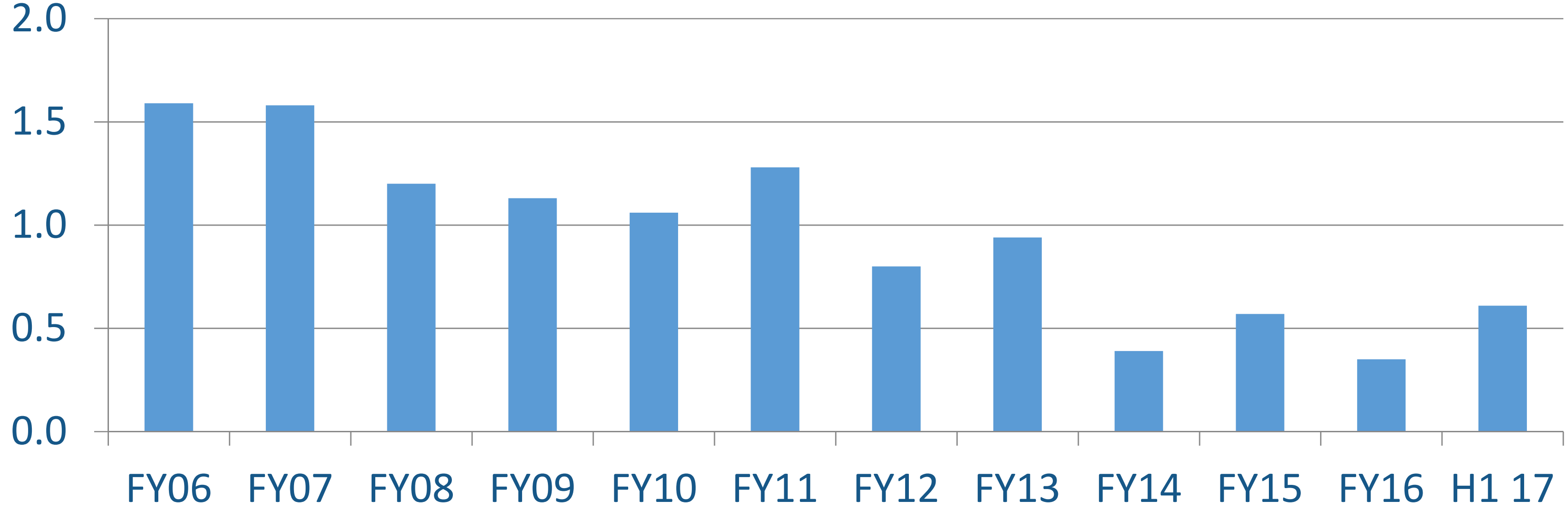
Safety

- Safety culture programmes remain key, every employee responsible for ensuring their peers are safe
- Systems and processes across Group to minimise exposure of employees to high hazard conditions
- Continued emphasis on reduction of risk in high hazard activities

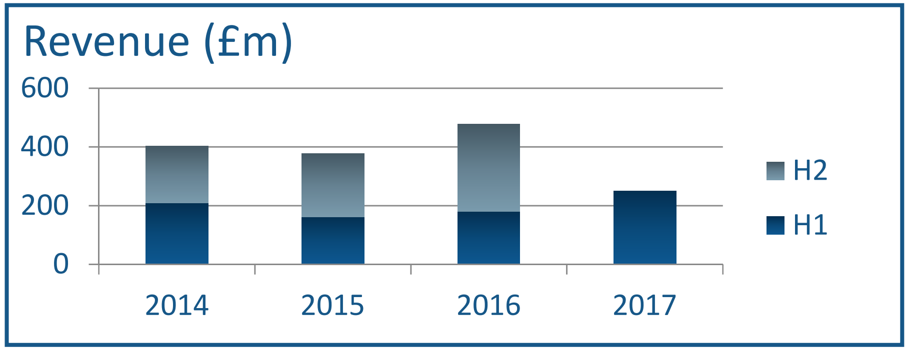


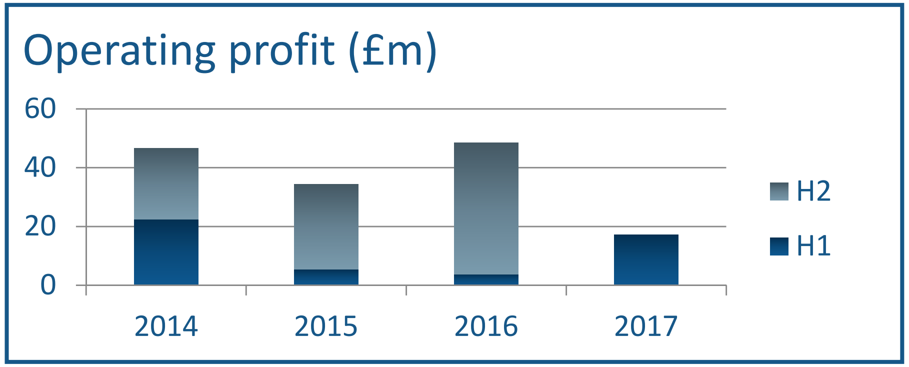
The figures above are the Lost Time Incident Rate (calculated using USA OSHA rules) per 100 employees per year.

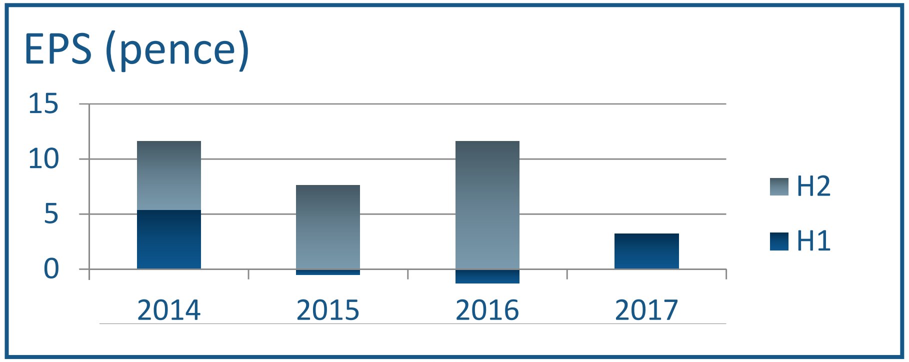
Financial Review

Andrew Lewis – Group Finance Director

Group performance







FINANCIAL HIGHLIGHTS

- Revenue up by 39%
- Operating profit growth of £13.4m to £17.2m
- EPS increased to 3.2p
- Return on sales up to 7%
- EBITDA/Revenue up to 12%
- Net debt at £112m reflecting investment in working capital in Energetics segment and supplier payment practices
- Dividend of 1.0p per share

OPERATIONAL HIGHLIGHTS

- Momentum of H2 2016 continued and customer deliveries made to plan
- Strong performance by Energetics, driven by both large contracts and the portfolio of smaller orders
- Order intake up 25% to £218m
- Closing order book of £556m
- H2 2017 expected revenue approximately 85% covered by order book

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Income statement

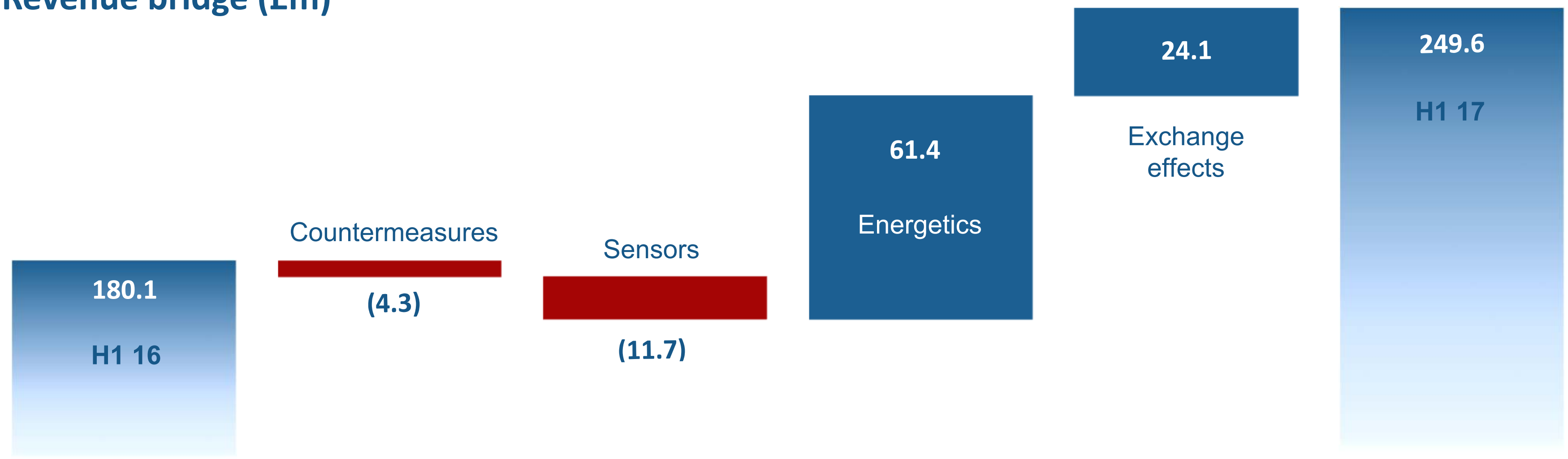
£m			H1 17	H1 16	FY16
Revenue	⬆	39%	**249.6**	180.1	477.1
Operating profit	⬆	353%	**17.2**	3.8	48.5
Finance expense	⬇	24%	**(5.9)**	(7.8)	(14.5)
Profit before tax			**11.3**	(4.0)	34.0
Tax rate			**21.2%**	22.5%	20.9%
Earnings per share			**3.2p**	(1.3)p	10.3p
Dividend per share			**1.0p**	-	1.3p

IFRS 15 has been adopted in H1 17. For further details, see appendix 7

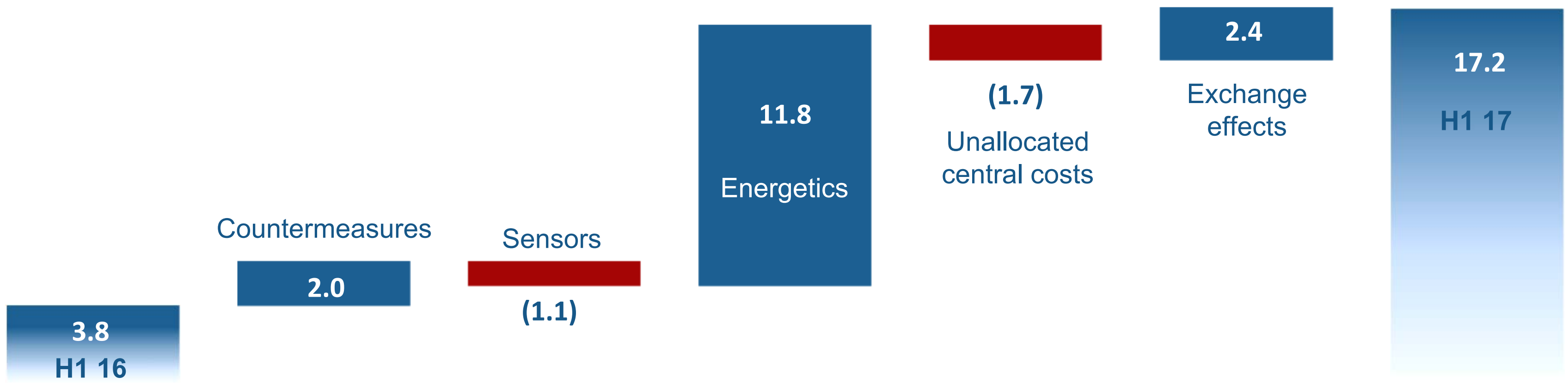
References to revenue, operating profit, finance expense, profit before tax and earnings per share are to underlying measures

Revenue and profit bridge

Revenue bridge (£m)



Operating profit bridge (£m)

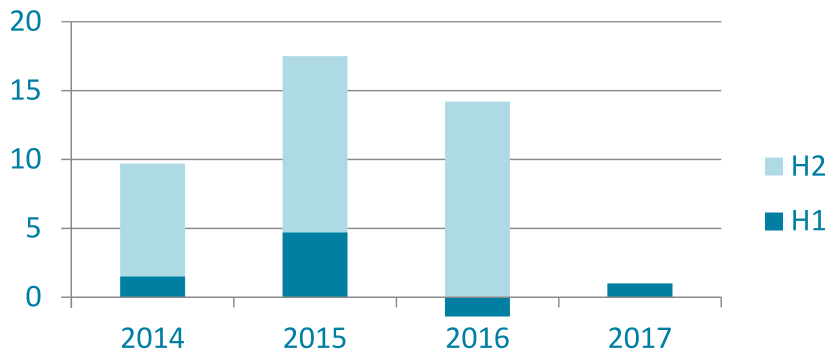


Countermeasures

			H1 17 £m	H1 16 £m	FY16 £m
Revenue	⬆	2%	**53.4**	52.2	138.3
EBITDA	⬆	67%	**7.0**	4.2	24.2
Operating profit			**1.0**	(1.4)	12.8
Operating margin			**1.9%**	(2.7)%	9.3%
Order book			**171.5**	171.5	177.0

- Plant 2 in Philadelphia closed with ramp up of modernised Plant 1 ongoing
- Strong performance in Australia
- F-35 programme progressing as expected
- US market outlook improving
- Closing order book of £172m, £78m for delivery in H2 2017, covering 91% of expected revenue

Operating profit (£m)



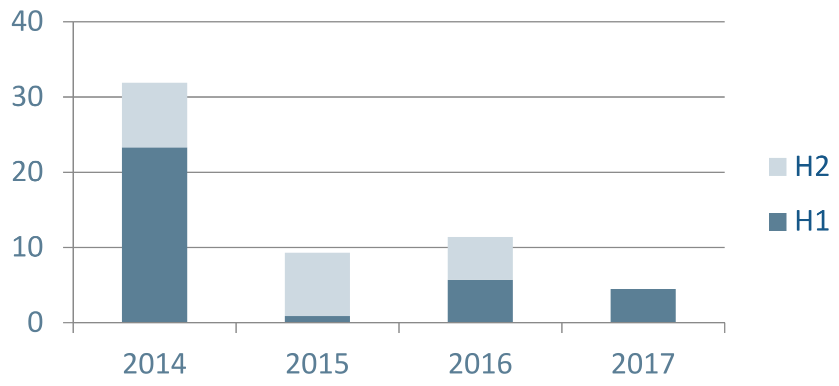
References to EBITDA, operating profit and operating margin are to underlying measures

Sensors

			H1 17 £m	H1 16 £m	FY16 £m
Revenue	⬇	20%	**40.3**	50.2	96.9
EBITDA	⬇	18%	**7.5**	9.2	18.0
Operating profit	⬇	21%	**4.5**	5.7	11.4
Operating margin			**11.2%**	11.4%	11.8%
Order book			**57.5**	91.5	49.3

- Cyber security budgets continue to grow
- HMDS orders received for fulfilment in H2 2017
- US business in R&D phase focused on Chemical & Biological Detection Programs of Record
- Strong performance in Land EW market
- Closing order book of £58m, £37m for delivery in H2 2017, covering 64% of expected revenue

Operating profit (£m)

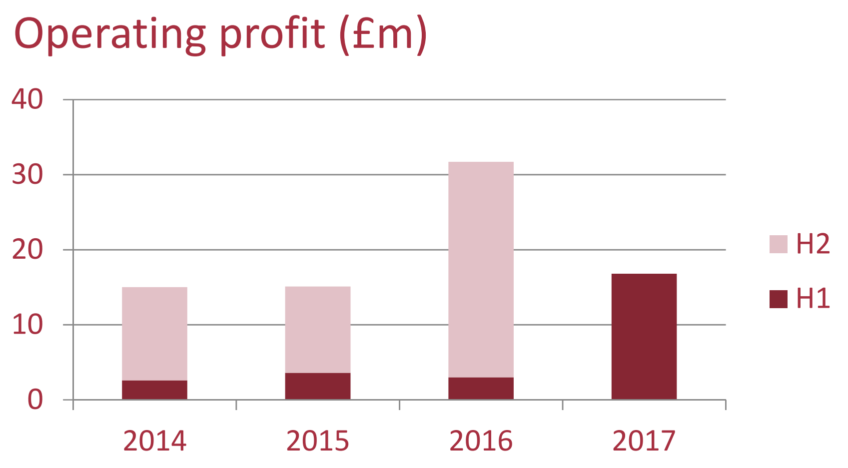


References to EBITDA, operating profit and operating margin are to underlying measures

Energetics

			H1 17 £m	H1 16 £m	FY16 £m
Revenue	⬆	101%	**155.9**	77.7	241.9
EBITDA	⬆	243%	**19.9**	5.8	37.6
Operating profit	⬆	460%	**16.8**	3.0	31.7
Operating margin			**10.8%**	3.9%	13.1%
Order book			**327.2**	328.3	366.6

- Strong performance across segment
- 40mm and NSA contracts performed well, funding confirmation expected shortly
- Portfolio of energetic devices growing, strong long term orders at Norway and Ardeer
- Torrance, CA site closure continues to plan, expected completion end FY18
- Closing order book of £327m, £144m for delivery in H2 2017, covering 91% of expected revenue



References to EBITDA, operating profit and operating margin are to underlying measures

Chemring Group

Impact of US $ translation

Group	Constant currency growth	H1 17 restated at 2016 rates £m	H1 16 £m	H1 17 £m
Revenue	25%	**225.4**	180.1	249.6
EBITDA	64%	**26.8**	16.3	30.0
Operating profit	289%	**14.8**	3.8	17.2
Order book	1%	**585.0**	591.3	556.2

TRANSLATION

- 64% of revenue US $ denominated in H1 2017
- P&L translation $1.26 vs $1.45 in H1 2016
- Balance sheet translation rate $1.29 vs $1.22 at FY16

SENSITIVITIES

- 5 cent stronger USD gives £1.2m increase in annual operating profit
- 5 cent stronger USD gives £4.2m increase in debt

References to EBITDA and operating profit are to underlying measures

Cash flow

£m	H1 17	H1 16	FY16
Cash flow before non-underlying items	**(7.9)**	7.4	81.4
Cash flow of non-underlying items	**(2.8)**	(7.2)	(8.1)
Cash flow from operations	**(10.7)**	0.2	73.3
Pension scheme deficit recovery contributions	**(2.5)**	(2.5)	(5.0)
Tax	**(3.3)**	(2.5)	(3.1)
Capital expenditure	**(8.2)**	(7.3)	(16.9)
Acquisitions	**-**	-	(2.5)
Finance expense	**(5.2)**	(7.0)	(11.9)
Amortisation of debt finance costs	**(1.2)**	(1.3)	(2.8)
Loan note early repayment costs	**-**	(4.5)	(5.1)
Net proceeds of share issue	**-**	76.0	75.4
Foreign exchange translation	**7.0**	(11.2)	(34.7)
Movement in net debt	**(24.1)**	39.9	66.7
Opening net debt	**(87.6)**	(154.3)	(154.3)
Closing net debt	**(111.7)**	(114.4)	(87.6)

- Investment in working capital in Energetics and to normalise supplier payment practices
- £29m repayment of PP loan notes in November 2016

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Balance sheet

£m	**H1 17**	H1 16	FY16
Goodwill & intangibles	**195.9**	194.6	210.0
Capitalised R&D	**36.6**	36.5	40.9
Property, plant & equipment	**169.7**	168.7	179.9
Working capital	**135.6**	112.0	108.3
Other	**(18.1)**	(19.8)	(20.8)
	519.7	492.0	518.3
Net debt	**(111.7)**	(114.4)	(87.6)
	408.0	377.6	430.7
Pension deficit	**(11.3)**	(17.4)	(17.3)
Net assets	**396.7**	360.2	413.4

- Net debt:EBITDA ratio of 1.37x
- £100m bank facility extended to July 2019. £53m of PP loan notes to be repaid November 2017
- Increase in working capital due to investment in Energetics and to normalise supplier payment practices, partially offset by collection of year end receivables

Chemring Group

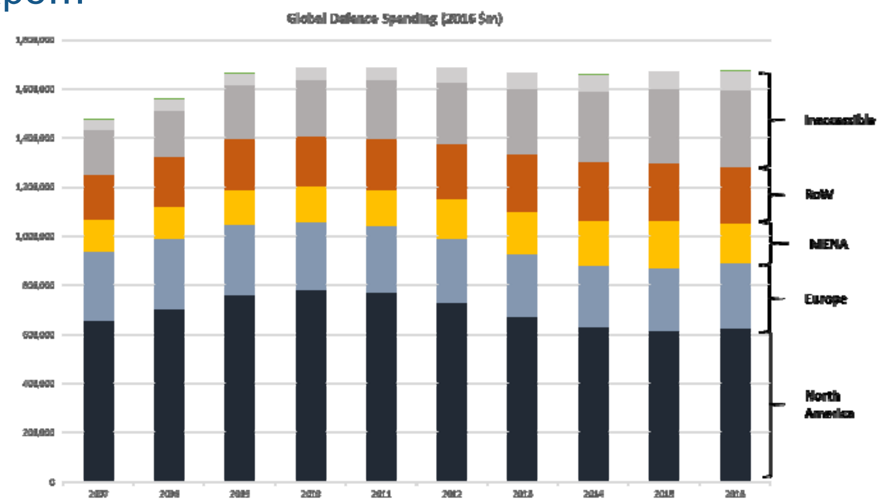
Chief Executive's Review

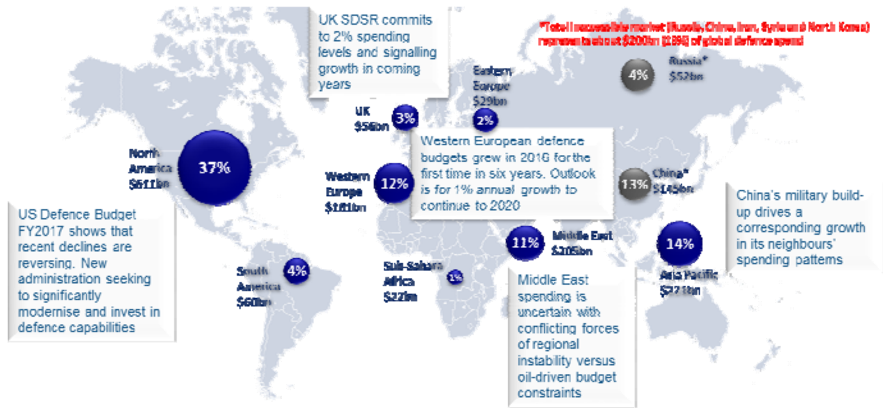
Michael Flowers

Positioned for growth

Against an increasingly uncertain geo-political landscape…

- NATO defence spending on an increasing trajectory
  - US administration in favour of significant modernisation and investment in defence capabilities
  - Increasing pressure on NATO members to commit to spending 2% of GDP on defence
- Middle East markets still challenging
- Nature of threat is changing. Nations must be prepared for nuclear, conventional and asymmetric threats, including chemical & biological attacks
- Increasing need for Chemring's long-term growth programmes





… Chemring is well positioned

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Progress on our roadmap

We continue to make good progress against operational improvements and against future growth programmes

Productivity	• Operational Excellence Programme underway - driving further improvements in safety, knowledge sharing, sales coordination, gross margins and cash generation
Site optimisation	• Plant consolidation at Alloy Surfaces completed post delivery of urgent requirements • Closure of Torrance facility in 2018 progressing according to plan • Minor sites closed at Charlottesville and Tallahassee
HMDS	• Upgrade programme realigned to incorporate spiral development, funding unchanged • Contract received for development, trials and manufacturing efforts in half. Significant further development and production contracts expected in 2018
JBTDS	• EMD phase ongoing • Milestone review Q3 followed by Government testing program, LRIP to follow
NGCD	• Prototype phase on all three variants. EMD phase to follow competitive tendering process • Initial tenders expected H2
F-35	• Low rate initial production continues to gradually gain momentum, LRIP 6 ongoing, LRIP 7 in award phase. F-35 SMD requirement in pre solicitation phase • Conclusion of second source qualification programme in Australia

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Operational Excellence Programme

Leveraging the synergies of the individual businesses through:

- a programme of disciplined collaboration, and
- the establishment of a culture of continuous improvement

Six operational excellence teams established to create a cohesive operational environment that delivers:

- greater customer satisfaction
- an empowered workforce
- superior shareholder value

Key H1 2017 achievements:

- Group level operational improvement initiatives at four sites
- Local improvement projects launched at each site
- Lean assessment tool developed and assessments complete
- Safety maturity assessment tool developed and assessments ongoing
- Group wide CRM system roll out commenced >50% complete, target 100% by year end
- UAE office opened as part of country management strategy

Disciplined capital allocation

Investment for growth remains the priority...

Capital allocation framework	
PP loan note repayment	• £117.2 million PP loan notes outstanding at Apr 2017 • £52.6 million repayment due in Nov 2017, remaining £64.6m Nov 2019
Investing to drive organic growth	• R&D c.£10.0 million per annum • Capex (maintenance and safety related) c.£15 million per annum • Capacity and capability enhancements at Norway and Kilgore • Operational excellence programme will drive increased capex for systems and improvement initiatives
M&A	• Targeted bolt-on acquisitions to fill capability gaps • Complementing existing technologies, factory footprints and routes to market
Dividend	• Board is committed to a sustainable dividend, seeking to grow the dividend over the long term, commensurate with other capital needs

…as we seek to maximise shareholder returns.

Emerging stronger from the downturn

The actions taken in recent years…

- Balance sheet strengthened
- Divestment of non-core assets
- Removal of divisional operating structure
- Bank facilities renegotiated
- Business unit integration and site closures
- Refreshed Board of Directors
- Bolt-on acquisitions
- Operational Excellence Programme launched
- Targeted operational and R&D investment
- Progress to a culture of continuous improvement and value creation

…have built a stronger platform for future growth.

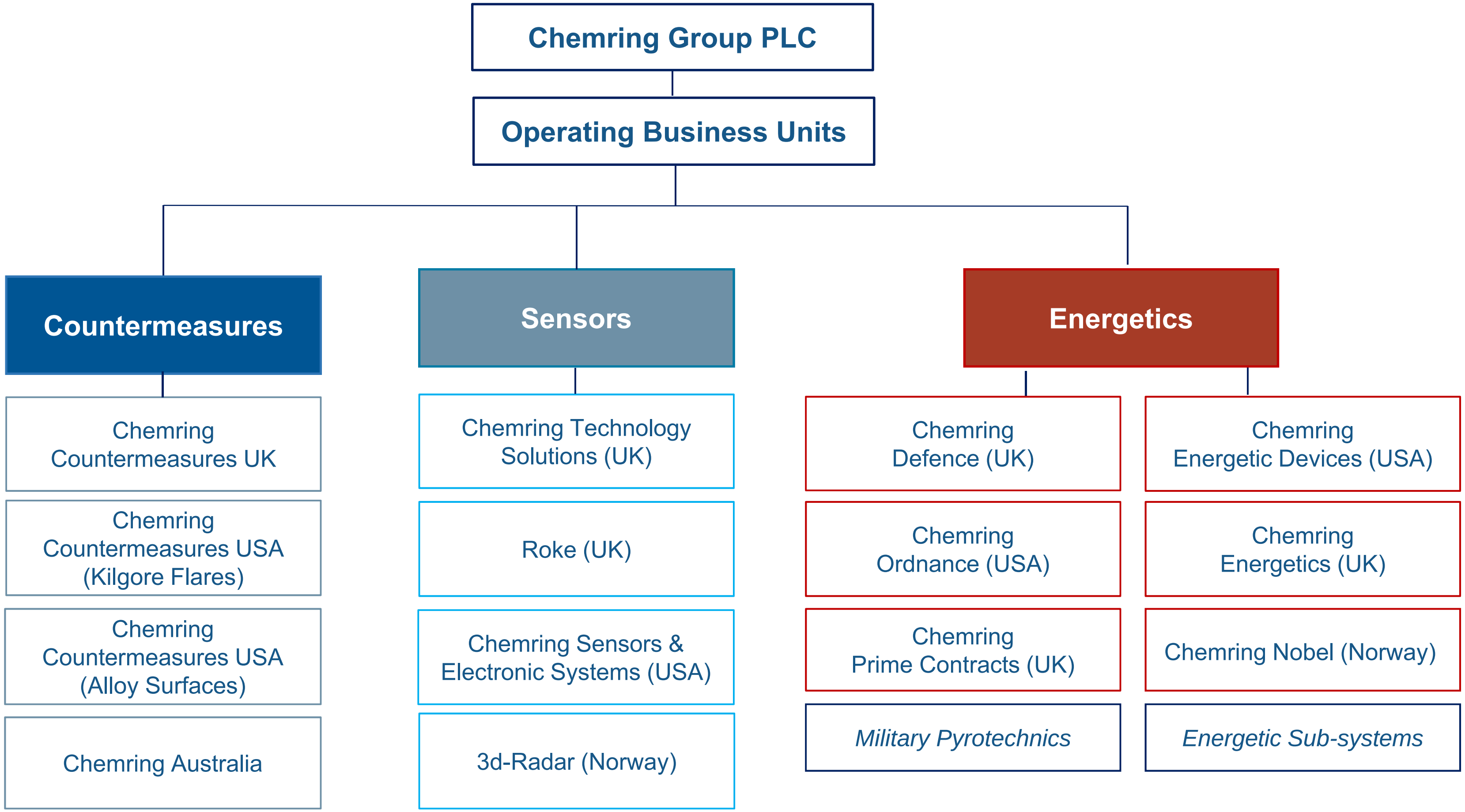
Summary and H2 Outlook

- Solid H1 performance across the Group
- Board's expectations for FY 2017 are unchanged
- Order book solid, approximately 85% of expected H2 revenue covered
- Safety remains an imperative
- Operational Excellence Programme progressing well with positive results already being seen
- Major growth programmes continue to progress, underpinning medium term opportunities
- Improving outlook for global defence spending

Q&A

Appendices

Appendix 1. Organisation chart



Appendix 2. Countermeasures

2017 Priorities	2017 H1 Performance
F-35 programme	Continue to deliver in support of initial US operational capability, second source development progressing
Kilgore operational improvement	Kilgore safety, waste reduction and margin improvement continues. Initial evaluation of modernisation plan completed
Alloy Surfaces consolidation	Alloy plant consolidation progressing, albeit delayed to meet urgent customer requirements. Completion expected H2 2017
New products	New naval round launched with significant orders from UK market, significant export interest. Major new customer in Middle East won, initial work in US market progressing

Appendix 3. Sensors

2017 Priorities	2017 H1 Performance
Counter-IED	Upgrade programme realigned to incorporate spiral development, funding unchanged
Next Generation Chemical Detection ("NGCD") R&D programme	Prototype phase on all three variants. EMD phase to follow competitive tendering process. Initial tenders expected Q3
Joint Biological Tactical Detection System ("JBTDS") R&D programme	EMD phase ongoing, all hardware deliveries complete. Milestone review Q3 followed by Government testing. LRIP to follow
Tactical Electronic Warfare	Sales continue to be strong with orders received from four new customers and six repeat customers
Roke	Opportunities continue to be progressed

Appendix 4. Energetics

2017 Priorities	2017 H1 Performance
Littoral Combat Ship Ammunition	Qualification contract awarded Progressing through USG qualification programme
Next Generation APOBS	Continue to complete technical and supply chain developments to ensure win on follow-on contract
Chemring Energetic Devices	Capability uplift at Downers Grove and transition out of Torrance continues to plan
40mm Systems	Significant contributor to H1 performance Funding for deliveries in H2 FY17 expected shortly
Portfolio Review	Ongoing High explosive capacity investment Make/buy analysis on critical supply chain elements complete

Appendix 5. Non-underlying items

H1 17 £m	P&L cost	Cash paid
Acquired intangibles amortisation	7.7	-
Business restructuring and incident costs	11.1	2.0
Claim related costs	0.2	0.4
Other items	(0.9)	-
	18.1	2.4
Disposal credits	(1.3)	0.4
	16.8	2.8

Appendix 6. Impact of US $ translation

Group	Constant currency growth	H1 17 restated at 2016 rates £m	H1 16 £m	H1 17 £m
Revenue	↑ 25%	**225.4**	180.1	249.6
EBITDA	↑ 64%	**26.8**	16.3	30.0
Operating profit	↑ 289%	**14.8**	3.8	17.2
Order book	↓ 1%	**585.0**	591.3	556.2

Countermeasures	Constant currency growth	H1 17 restated at 2016 rates £m	H1 16 £m	H1 17 £m
Revenue	↓ 8%	**47.9**	52.2	53.4
EBITDA	↑ 45%	**6.1**	4.2	7.0
Operating profit		**0.5**	(1.4)	1.0
Order book	↑ 5%	**180.6**	171.5	171.5

Sensors	Constant currency growth	H1 17 restated at 2016 rates £m	H1 16 £m	H1 17 £m
Revenue	↓ 23%	38.5	50.2	40.3
EBITDA	↓ 18%	7.5	9.2	7.5
Operating profit	↓ 18%	4.7	5.7	4.5
Order book	↓ 35%	59.4	91.5	57.5

Energetics	Constant currency growth	H1 17 restated at 2016 rates £m	H1 16 £m	H1 17 £m
Revenue	↑ 79%	**139.0**	77.7	155.9
EBITDA	↑ 203%	**17.6**	5.8	19.9
Operating profit	↑ 390%	**14.7**	3.0	16.8
Order book	↑ 5%	**345.0**	328.3	327.2

References to EBITDA and operating profit are to underlying measures

Appendix 7. IFRS 15

The Group has adopted IFRS 15 for its 2017 financial year. The Group has taken advantage of the modified transitional provisions and as such the 2016 results remain as previously reported. A summary of the impact of this adoption on the H1 2017 results is shown below:

Continuing operations (£m)	**Pre IFRS 15**	**IFRS 15 adjustment**	**As reported**
Revenue	235.3	14.3	249.6
Operating profit	13.1	4.1	17.2
Finance expense	(5.9)	-	(5.9)
Profit before tax	**7.2**	**4.1**	**11.3**
Tax charge	(1.5)	(0.9)	(2.4)
Profit after tax	**5.7**	**3.2**	**8.9**

In addition, a number of transactions, with a broadly equivalent operating profit impact, will now be recognised in the second half of 2017 that could have previously been recognised in the first half. This timing difference is expected to recur at each reporting period end, albeit at a different quantum.

Appendix 8. Working capital

£m	H1 17	H1 16	FY16
Inventories	**113.3**	111.8	104.8
Receivables	**74.5**	57.1	105.7
Trade payables	**(36.5)**	(40.5)	(64.1)
Advance receipts from customers	**(38.8)**	(11.5)	(43.4)
Advance payments to suppliers	**36.5**	10.4	27.6
Other items	**(13.4)**	(15.3)	(22.3)
	135.6	112.0	108.3

Appendix 9. Glossary

APOBS	Anti-Personnel Obstacle Breaching System
CED	Chemring Energetic Devices
CHG	Chemring Group
EMD	Engineering and Manufacturing Development
EW	Electronic Warfare
F-35	F-35 Joint Strike Fighter
FMS	Foreign Military Sales
HMDS	Husky Mounted Detection System
IDIQ	Indefinite Delivery Indefinite Quantity
IED	Improvised Explosive Device
JBTDS	Joint Biological Tactical Detection System
LRIP	Low Rate Initial Production
MTV	Magnesium Teflon Viton
NASA	National Aeronautics Space Administration
NGCD	Next Generation Chemical Detector
NSA	Non Standard Ammunition
RN	Royal Navy
SMD	Special Material Decoy
US DoD	United States Department of Defense
USG	United States Government
3d-R	3d Radar

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