

Chemring Group PLC

Results for the year ended 31 October 2016

Key points

Revenue

£477.1 million, up 26.5% with growth in Energetics and countermeasures
Constant currency revenue £440.3 million, up 16.7%

Operating profit*

£48.5 million, up 41.0% with good performance from Energetics segment
Constant currency operating profit £43.0 million, up 25.0%

Safety

Lost time incident rate lowest on record

Progress

Good cash conversion - operating cash flow £76.4 million
Net debt £87.6 million (Oct 15: £154.3 million)
Strengthened balance sheet post rights issue
40mm contract fully effective
Continued progress on long-term Sensor programmes and F-35
Site rationalisation and restructuring projects continuing
Dividend reinstated

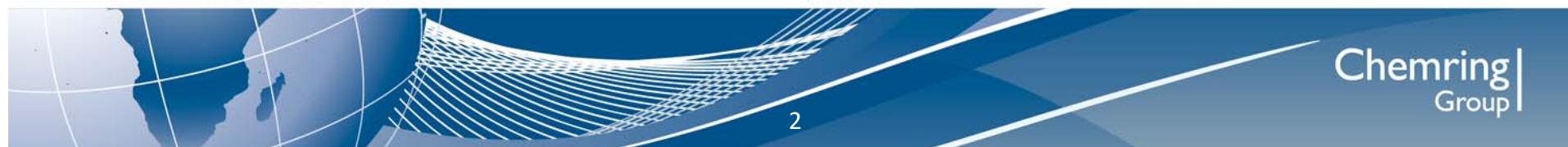
Order book

£592.9 million, up 4.1%, of which £368.0 million is currently expected to be recognised as revenue in FY17

FY17 outlook

Board's expectations for FY17 unchanged, based on current FX rates
H2 weighted

* References to operating profit are to underlying measures

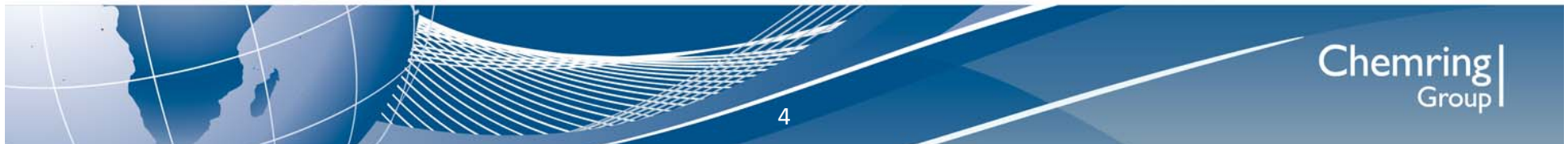


Safety

- FY16 Lost time incident rate is the lowest on record, reflecting enhanced culture and investment in safety
- Systems and processes in place across Group to minimise exposure of employees to high hazard conditions
- Continued emphasis on reduction of risk in high hazard activities
- Safety culture programs remain key, every employee responsible for ensuring their peers are safe
- Significant effort over forthcoming period to reduce to As Low As Reasonably Practicable (ALARP) personnel exposure to potentially lethal hazards

Financial Review

Andrew Davies – Deputy Group Finance Director



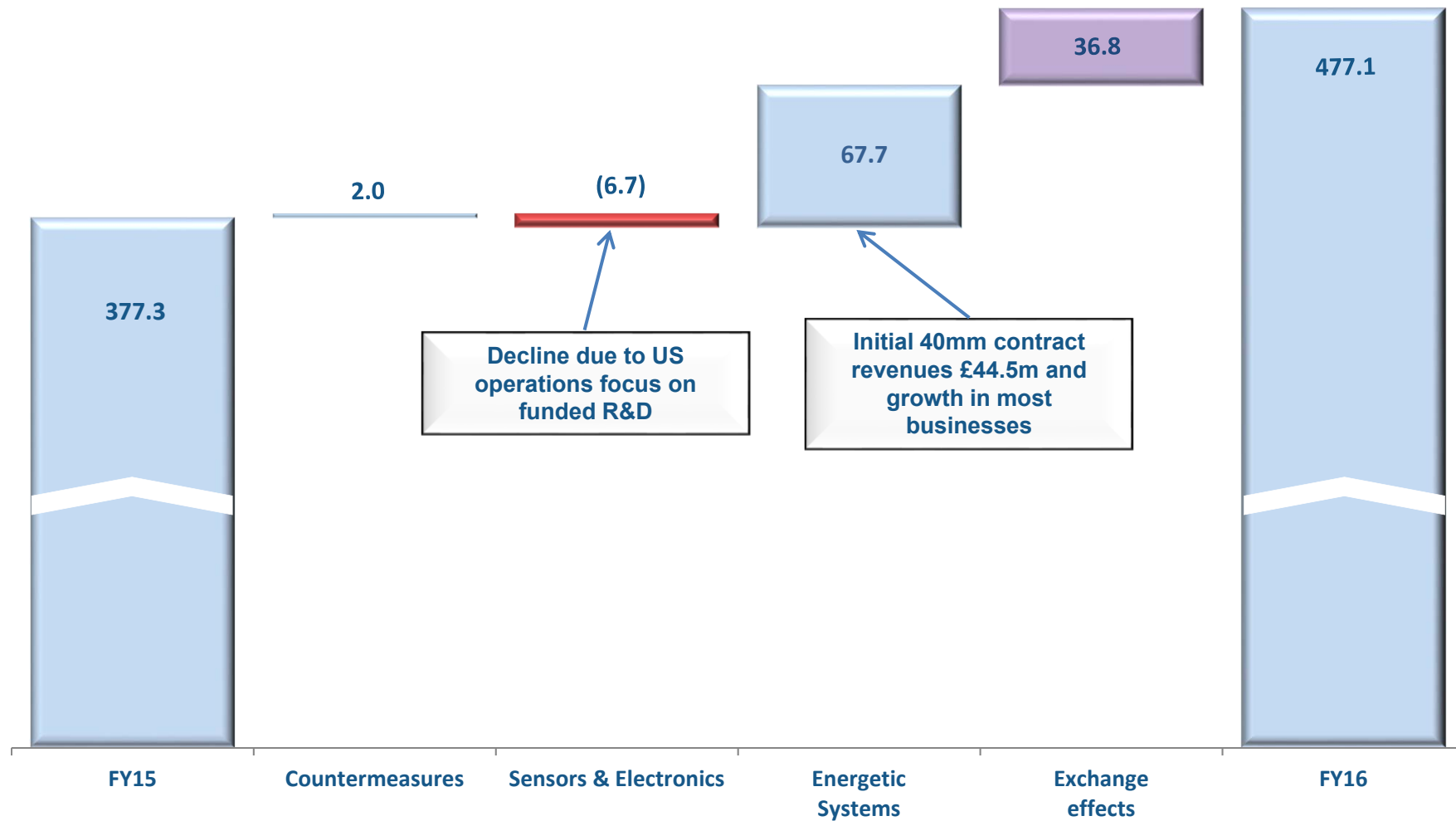
FY16 Results

		FY16		FY16 constant currency	FY15
Revenue	+26.5%	£477.1m	+16.7%	£440.3m	£377.3m
Operating profit*	+41.0%	£48.5m	+25.0%	£43.0m	£34.4m
Operating margin*		10.2%			9.1%
Profit before tax*	+71.7%	£34.0m	47.0%	£29.1m	£19.8m
Earnings per share*	+45.1%	10.3p			7.1p**
Interim dividend per share		-			2.1p**
Final dividend per share		1.3p			-
Net debt	-43.2%	£87.6m	-57.7%	£65.2m	£154.3m
Order book	+4.1%	£592.9m	-14.0%	£489.8m	£569.6m

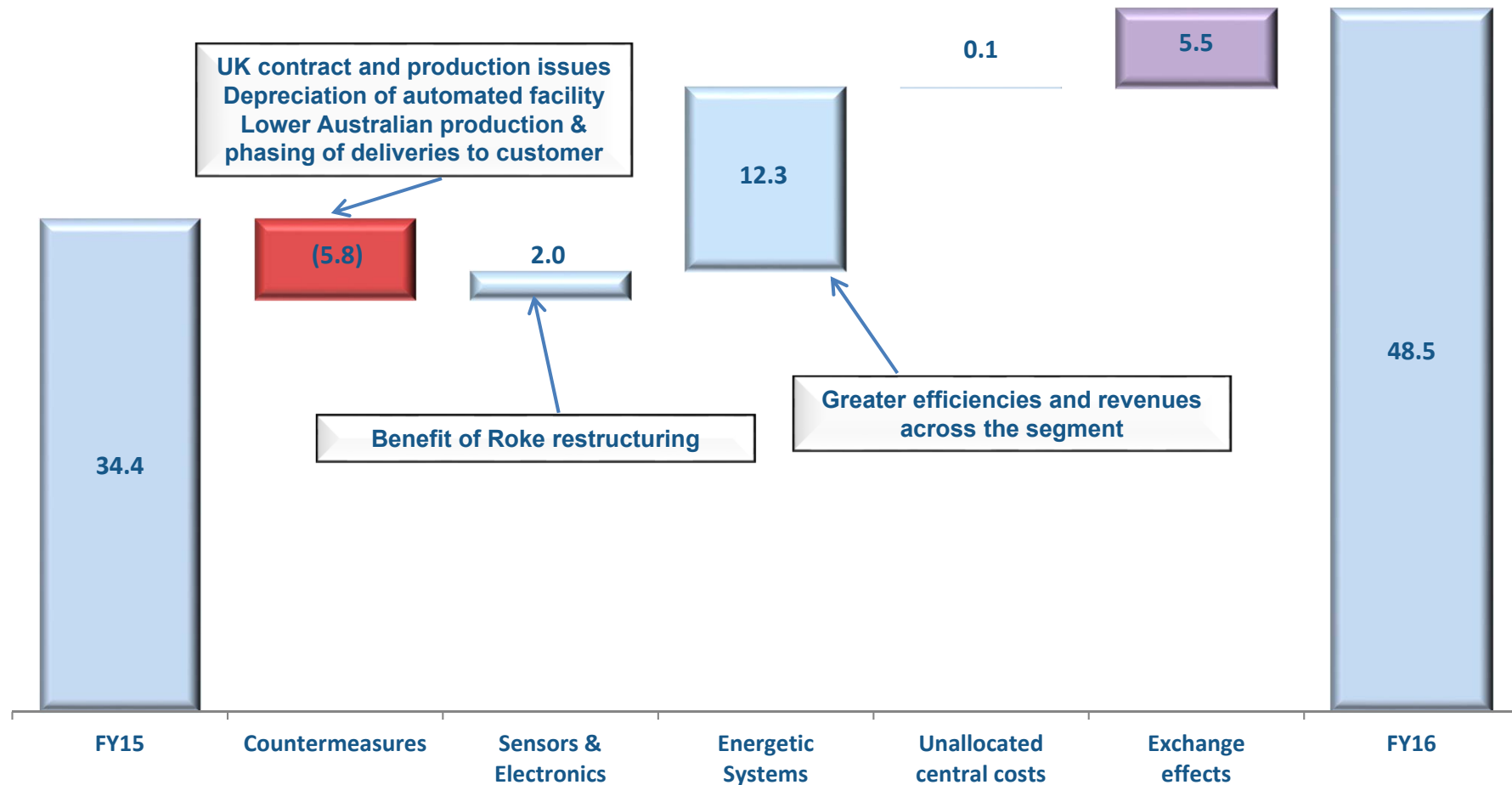
* References to operating profit, profit before tax and loss per share are to underlying measures

** Restated 2015 earnings per share to reflect bonus element of rights issue during the year

Revenue bridge



Operating profit bridge

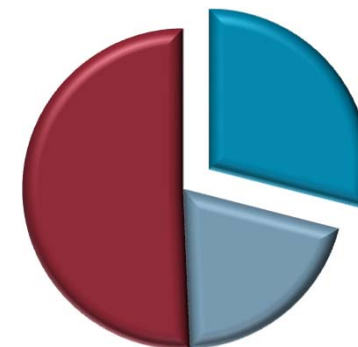


References to operating profit is to underlying measure

Countermeasures

	FY16	<i>FY16 Constant currency</i>	FY15	Change
Revenue	£138.3m	£127.8m	£125.8m	+9.9%
Operating profit*	£12.8m	£11.7m	£17.5m	-26.9%
Operating margin*	9.3%	9.2%	13.9%	
Order book	£177.0m	£147.4m	£184.1m	-3.9%

29% of Group Revenue



FY16 review

Continued recovery in the segment with increased revenues

Manufacturing issues in UK and incidents in US and Australia reduced profits

Order book decline reflects improving production consistency in US

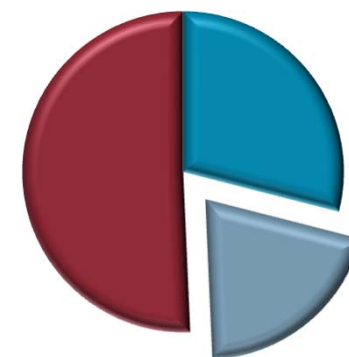
Orders received for both F-35 operational and training flares, and newly developed special materials flare

* References to operating profit and operating margin are to underlying measures, which are reconciled to statutory figures at Appendix 1

Sensors & Electronics

	FY16	<i>FY16 Constant currency</i>	FY15	Change
Revenue	£96.9m	£92.4m	£99.1m	-2.2%
Operating profit*	£11.4m	£11.3m	£9.3m	+22.6%
Operating margin*	11.8%	12.2%	9.4%	
Order book	£49.3m	£43.2m	£75.8m	-35.0%

20% of Group Revenue



FY16 review

US activity still focused on lower margin R&D for US DoD

Good progress on all three streams of NGCD Program of Record

First shipments of new hand-held IED detector products. Major EW order from Australia

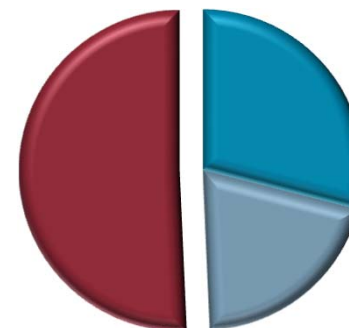
Year on year profit growth at the Roke cyber and security business following restructuring in FY15

* References to operating profit and operating margin are to underlying measures, which are reconciled to statutory figures at Appendix 1

Energetic Systems

	FY16	<i>FY16 Constant currency</i>	FY15	Change
Revenue	£241.9m	£220.1m	£152.4m	+58.7%
Operating profit*	£31.7m	£27.4m	£15.1m	+109.9%
Operating margin*	13.1%	12.4%	9.9%	
Order book	£366.6m	£299.2m	£309.7m	+18.4%

51% of Group Revenue



FY16 review

All but one business reported growth in revenue and profits in the year

40mm contract continues to perform well adding £44.5m of revenue in year

Site consolidation plan for Chemring Energetic Devices in USA commenced. Restructuring at Chemring Defence

* References to operating profit and operating margin are to underlying measures, which are reconciled to statutory figures at Appendix 1

Income statement

Interest	£m	FY16	FY15
£1.8m reduction in interest cost due to prepayments of loan notes offset by adverse exchange rate effect	Operating profit*	55.9	41.9
	Corporate costs	(7.4)	(7.5)
	Operating profit	48.5	34.4
Tax	Interest	(14.5)	(14.6)
Consistent effective tax rate	Profit before tax	34.0	19.8
Earnings per share			
Shares in issue 261.4m			
Dividend	Tax rate	20.9%	20.7%
Dividends to re-start	Earnings per share*	10.3p	7.1p**
	Dividend per share	1.3p	2.1p**

* References to operating profit, (loss)/profit before tax and loss per share are to underlying measures

** Restated 2015 earnings per share to reflect bonus element of rights issue during the year

Non-underlying items

Debt repayment and accelerated interest costs

Interest due on early repayment of loan notes and associated covenant amendment fees

Business restructuring and incident costs

US plant closures and UK headcount reduction

Acquisition and disposal credit

Release of provisions relating to prior year disposals

Claim-related credit

Cash paid in relation to historic claims, fully accrued for in FY15

FY16	P&L	Cash
£m	Cost	paid
Acquired intangibles amortisation	14.8	-
Debt repayment costs	1.4	1.4
Accelerated interest costs	3.7	3.7
	19.9	5.1
Business restructuring and incident costs	5.4	2.8
Acquisition and disposal credit	(4.4)	0.3
Claim-related credit	(0.6)	5.0
Other items	1.0	-
	21.3	13.2

Balance sheet

Capitalised R&D

Includes £14.9m investment relating to long-term US chemical & biological detection programmes

Working capital

See next slide

Bank covenant

Net debt : EBITDA 1.15x
(Limit 3.00x)

£m	FY16	FY15
Goodwill & intangibles	210.0	195.4
Property, plant & equipment	179.9	168.0
Capitalised R&D	40.9	36.1
Working capital	99.1	81.8
Tax	(2.0)	(5.5)
Pension deficit	(17.3)	(17.7)
<i>Gross debt</i>	(150.7)	(161.9)
<i>Cash</i>	63.1	7.6
Net debt	(87.6)	(154.3)
Other	(9.6)	(13.2)
Net assets	413.4	290.6

Working capital

£21.0m of increase FX related

WC on constant currency basis
£78.1m

Inventories

Down 9.5% on constant currency
basis at £87.1m, reflecting actions
during the year

Trade receivables

Increase reflecting strong Q4
trading

Prepayments

Increase due to advanced supplier
payments made by Chemring
Ordnance to secure production on
Middle East contracts

Trade Payables

Increase reflecting strong Q4
trading and year end cash
management

£m

	FY16	FY16 <i>constant currency</i>	FY15
Inventories	104.8	87.1	96.2
Trade receivables	82.7	70.5	66.1
Contract receivables	7.0	7.0	15.2
Prepayments	22.0	15.5	6.8
Trade payables	(53.5)	(44.9)	(46.7)
Advance payments	(12.4)	(10.1)	(11.5)
Other items	(51.5)	(47.0)	(44.3)
	99.1	78.1	81.8
Revenue	477.1	440.3	377.3
WC % of revenue	20.8%	17.8%	21.7%

Operating cash flow

	£m	FY16	FY15
Depreciation			
Increased depreciation from Countermeasures UK automated facility	Operating profit	48.5	34.4
	Depreciation	18.4	16.3
	Loss on fixed asset disposals	0.2	0.3
Pension	Amortisation	6.9	6.4
Funding £5m pa until June 2019	Pension contributions	(5.0)	(5.0)
	Other	1.0	1.2
Working capital		70.0	53.6
Net inflow reflects inventory decrease (on constant currency basis)	Inventory	13.6	(19.1)
	Debtors	(5.8)	(3.1)
	Creditors & provisions	(1.4)	4.0
Cash conversion rate	Working capital change	6.4	(18.2)
123% (FY15 : 53%) (after adjusting for Capex)*	Operating cash flow	76.4	35.4

* Operating cash conversion is cash generated from underlying operations, less purchases of intangible assets, property, plant & equipment, and proceeds on disposal, as a percentage of underlying profit

Modelling considerations

FY17 Income statement

- H1:H2 revenue split expected to improve to broadly 40:60 for FY17. Greater H2 profit weighting expected due to operational gearing
- 40mm ammunition contract (Energetics) anticipated to provide a significant contribution during FY17 and H1 FY18
- USD rate effect minor - 1¢ stronger USD adds £0.2m to PBT on FY16 activity levels
- 2016 average USD/GBP translation rate 1.28 (2015 : 1.53)
- FY17 outlook based on USD/GBP translation rate of 1.25
- Underlying interest expected to be c.£12m
- Tax rate stable at c.21%

FY17 Balance sheet

- USD rate effect - 1¢ stronger USD gives c.£0.9m higher debt on FY16 balance sheet
- 2016 closing USD/GBP translation rate 1.22 (2015 : 1.54)
- Capex to run in line with depreciation
- Capitalised R&D to run in line with amortisation, reducing thereafter as US Sensors & Electronics projects complete

Chief Executive's Review

Michael Flowers

Our market strategy

Position for growth through innovation, manufacturing excellence and international expansion

Countermeasures



- Strengthen position on key programs: Typhoon and F-35
- Improve position in Naval countermeasures market
- Continue focused R&D effort
- Investment in operational processes

Sensors & Electronics



- Focus on areas of technological strength in counter-IED, Electronic Warfare, and chemical and biological detection
- Increase technology lead through customer funded and internally funded R&D
- Win key NATO programmes to exploit globally
- Roke to grow, particularly in cyber and security applications

Energetic Systems



- Maintain current business base and product range whilst seeking new markets
- Broaden into adjacent commercial markets
- Growth focus on higher technology niche aerospace, space and missile system applications

Our segmental strategies

**Chemring
Group**

**Deliver profit
and cash**

**Embed
operational
excellence**

**Invest for
growth**

Countermeasures

Complete restructuring and
site rationalisations

Operational excellence
programme

Targeted facilities investment

Secure F-35 flare
Broaden naval countermeasure
business

Sensors – Products

Rationalise sites and manufacturing operations

Targeted R&D investment to secure Growth
Programmes

– Roke

Recruit to meet current demand
Enhance internal development capability for cyber and
security professionals

Establish satellite offices

Energetics

Deliver current order book

Operational excellence
programme

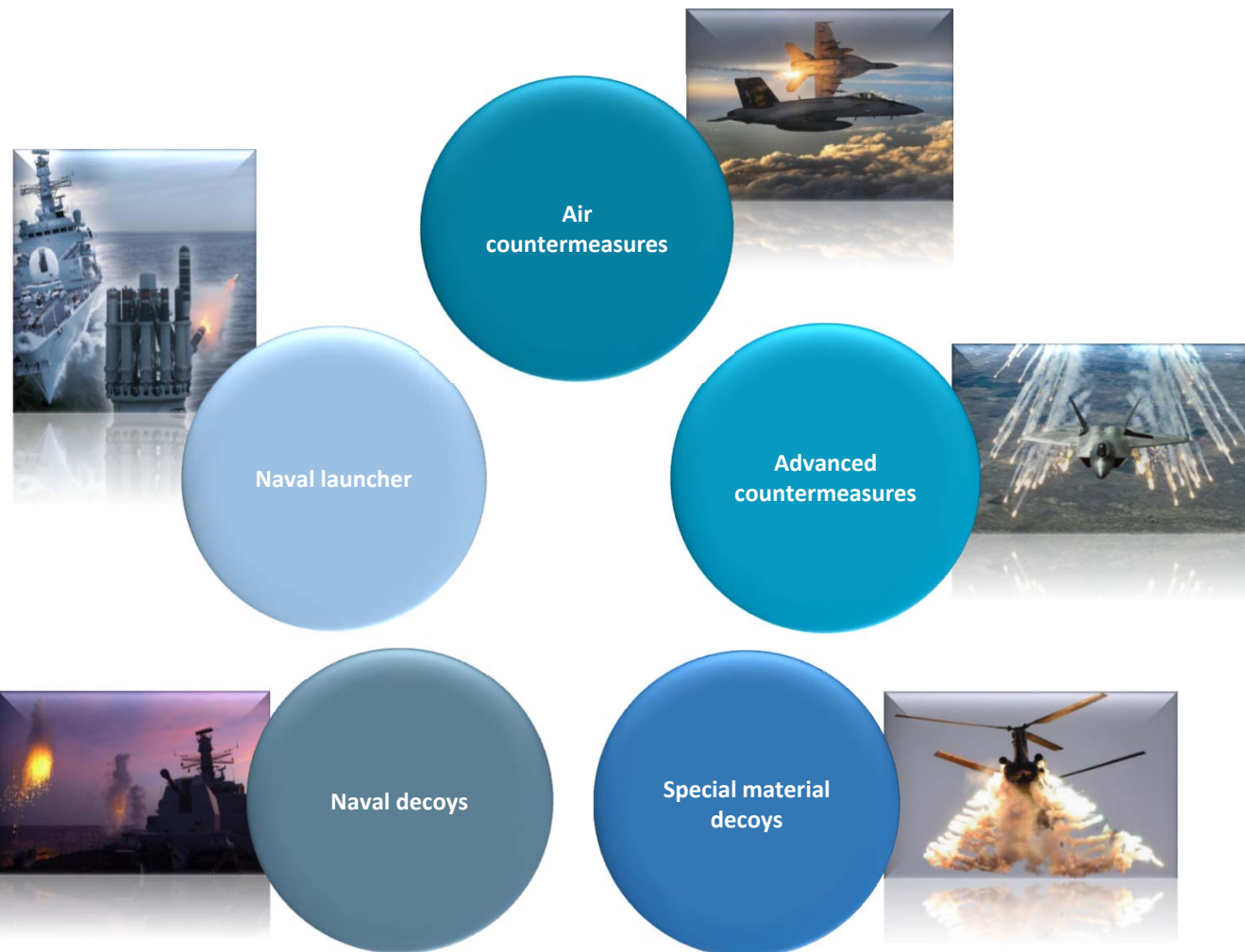
Deliver cash to fund growth
Focus segment on higher
margin niche products

Complete restructuring and site
rationalisation

Exploit synergies in internal
supply and routes to market

**Chemring
Group**

Countermeasures



Countermeasures

2016 Performance

F-35 - LRIP 5 contract delivered, LRIP 6 contract awarded. Training flare contract awarded. Australian second source qualification nearing successful completion

Kilgore - Safety performance and waste management improved. Overhead reducing, down 9% 2015 – 16, targeted 20% reduction in FY17. Operational performance still lagging

Alloy Surfaces - plant consolidation progressing, final closure will be delayed until end H1 FY17 due to urgent customer requirements. New SMD countermeasure launched

Naval Countermeasure - New naval round launched with orders from UK market, significant export interest. Major new customer in Middle East won, initial work in US market progressing

Collaboration - Greater alignment in all operations. First UK manufactured flare trialled by US customer

Countermeasures

2017 Priorities

F-35 - Deliver LRIP 6 in support of F-35 programme, conclude Australian qualification program, and conclude Year 1 deliveries of F-35 training flare

Kilgore - Undertake detailed planning for implementation of Kilgore 5 year investment program aimed at enhancing overall safety, operational performance and customer delivery

Alloy - Conclude consolidation of Plants 1 and 2. Fully introduce into service new design SMD countermeasures. Progress technology diversification programs

New products - Deliver new design Naval countermeasure to RN, incorporating new CHG rocket motor. Progress US naval market. Progress development of advanced spectral and MTV countermeasures

FY17 Outlook – Trading performance, while underpinned by a good order book, is expected to be slightly down year on year, as production will be impacted by US site consolidation activities in H1. US demand remains subdued but F-35 programme increasing in momentum

Sensors & Electronics

Counter IED &
Explosive
Ordnance
Disposal



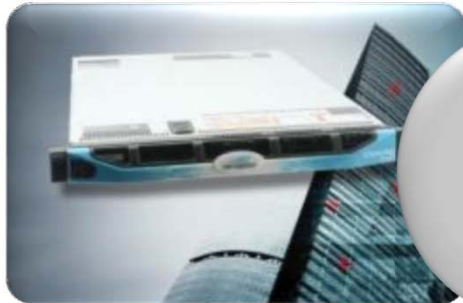
Chemical &
biological
detection



Electronic
warfare



Security



Sensors & Electronics

2016 Performance

HMDS - Funded development ongoing, initial order for trials hardware expected Q1. Export order for advanced capability received

NGCD - All three prototype systems in test

JBTDS - Final testing of prototypes commenced, initial results promising

Hand-held - c.\$10m orders received for hand-held IED detectors ex US. Initial orders for complementary systems developed in UK received. Development contract received ex Australia

International HMDS & 3d-R sales - Opportunities continue to be progressed, results remain below expectations

Electronic Warfare - Major order received from Australia, two new NATO customer orders received. Secured upgrade and repeat orders for existing customers

Collaboration - UK technology incorporated into HMDS solution

Sensors & Electronics

2017 Priorities

Counter-IED – Deliver initial enhanced capability HMDS hardware to USG and continue spiral development. Progress FMS and commercial sales of HMDS, 3d-R and hand-held solutions to export customers. Funded R&D enhancements in support of Australian and USG hand-held customers

Next Generation Chemical Detection – Progress through prototype testing into EMD phase of system post competitive tendering process

Joint Biological Tactical Detection System – Conclude EMD phase, moving into LRIP in year

Tactical Electronic Warfare – Delivery of major system orders whilst concurrently undertaking system development to meet emerging requirements. Expand country of use footprint

Roke – Further grow business base and staff utilisation. Establish improved internal cyber skills staff development program. Grow second operational site (Gloucester)

FY17 Outlook – Trading expected to benefit from the continued improvement in profitability from the UK businesses, primarily in EW and Cyber. US R&D activities transition to EMD and LRIP phases as the year progresses

Energetic Systems



Military
pyrotechnics

Space and
missile
components



Demolition
stores



Mine & obstacle
breaching
systems



Aircrew egress /
safety



Energetic Systems

2016 Performance

40mm - First deliveries in April, routine deliveries ongoing. Ramp up achieved faster than expected, with throughput and yield at planned levels

5yr NSA IDIQ - Won, orders of \$160m received in 2016. Further orders of \$45m received since FY16 year end

CED site rationalisation - Ongoing to plan. No new orders accepted into Torrance, only 21 live contracts remain. NASA Standard Initiator qualification (most significant element) progressing to plan

Improve Nobel performance - Activity ongoing. Yield in Q4 above historical levels. Record profitability

Implement systems to improve production and working capital management

- New system fully operational at Chemring Defence
- Chemring Energetics implementation to complete in Q1 2017, ongoing slippage has been disappointing

Energetic Systems

2017 Priorities

Littoral Combat Ship Ammunition – Progress through USG qualification programme on niche ammunition requirements

Next Generation APOBS – Complete necessary technical and supply chain developments to ensure win on follow on APOBS contract

40mm Systems – Continue delivery of legacy systems, whilst focussing on USG and export requirements for niche specialist ammunition types

Chemring Energetic Devices – Progress closure of Torrance site. Grow in space, missile and aerospace applications market. Develop non-explosive device market

Portfolio Review – Undertake review of energetics product and capability portfolio and optimise in line with higher margin niche and specialist market strategy

FY17 Outlook – trading expected to be solid, with the segment benefiting from a strong order book, and improved delivery performance across the segment

Operational Excellence Programme

Launched in late 2016 to unlock potential for significant further improvement and embed excellence. Activity will focus on:

- Safety
- Manufacturing operations performance
- Group-wide sales effectiveness and coordination
- New product development
- Enhancing engineering capability
- Procurement
- Talent management and development
- Commercial contracting and legal

Our medium-term ambitions

- No one exposed to lethal hazards – no life altering injuries
- Achieve benchmark margins across all business sectors
- Enhanced working capital management delivering year on year improvement
- Solid balance sheet with flexibility for organic or acquisitive investment as needs and opportunities arise
- Collaborative environment
- Culture of continuous improvement and innovation
- Employer of choice with a talented, motivated and incentivised workforce

Summary and FY17 Outlook

- Safety performance continues to improve
- Market conditions have stabilised at macro level, global geopolitical environment very uncertain
- Cost base has been rationalised, with all Divisional HQs closed, business overheads cut, and plant consolidations nearing conclusion
- Operational performance continues to improve
- Order book solid. £368.0 million of current order book is expected to be recognised as revenue in FY17
- Transition from operational restructuring and cost rationalisation to operational excellence
- Board's expectations for FY17 unchanged, based on current FX rates
- Medium term prospects positive - important year for HMDS, NGCD and JBTDS as programmes move into engineering and manufacturing development or low rate initial production phases

Questions

Appendices

Appendix 1. Movement in net debt

	£m	FY16	FY15
Rights Issue			
Net cash inflow £75.4m	Operating cash flow	76.4	35.4
Change in net debt	Non-underlying items	(8.1)	(8.4)
Excluding rights issue, net debt up £8.7m, driven by:	Capex	(10.3)	(8.2)
- £34.7m exchange rate effects – translation of USD debt at \$1.22 (Oct 15: £1.54)	Capitalised R&D	(6.7)	(8.9)
- £6.4m working capital inflow	Interest	(11.9)	(11.8)
- £5.1m non-underlying accelerated interest costs and fees	Tax	(3.1)	(1.3)
Capex	Dividends	-	(7.9)
Spend continues to be focused on modernising production facilities	Share issue (net of costs)	75.4	-
Capitalised R&D	Accelerated interest and debt fees paid	(5.1)	-
Investment centred on Sensors & Electronics	Others	(5.2)	(2.1)
	Exchange rate effects	(34.7)	(5.5)
	Movement in net debt	66.7	(18.7)
	Net debt b/f	(154.3)	(135.6)
	Net debt c/f	(87.6)	(154.3)

Appendix 2. Debt funding and covenants

Revolving Credit Facility

£100m, committed to July 2018

Loan notes

£48.8m of loan notes repaid from rights issue proceeds

£153.4m outstanding at Oct 16

First repayment £29.5m, paid in Nov 2016

£55.4m due for repayment in Nov 2017 and £68.5m in Nov 2019

Covenant position considerably more robust

October 2016

Actual Covenant

Revolving Credit Facility

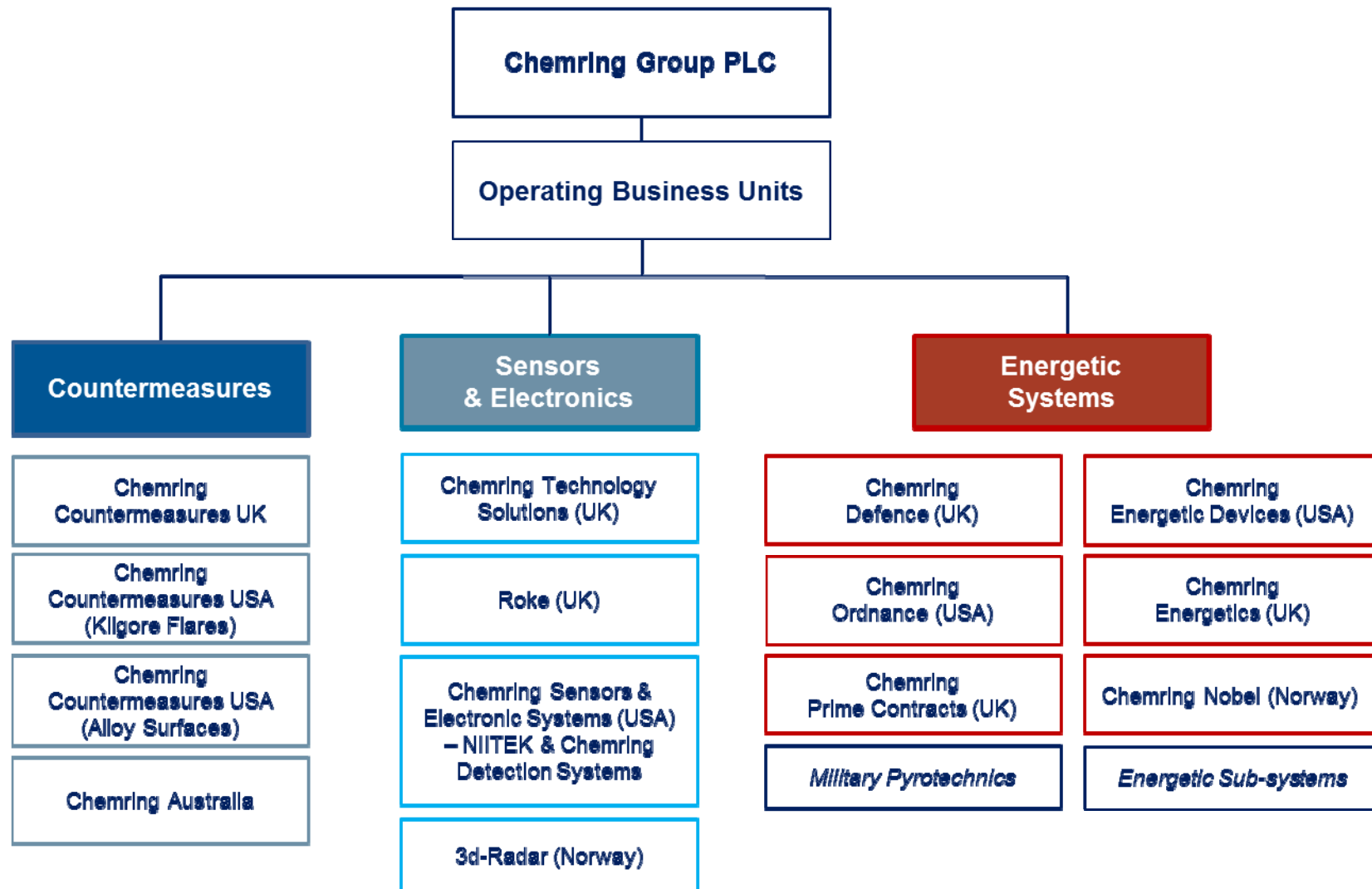
Leverage - net debt to EBITDA	1.15x	<3.00x
Interest cover	6.82x	>4.00x

Loan notes

Leverage

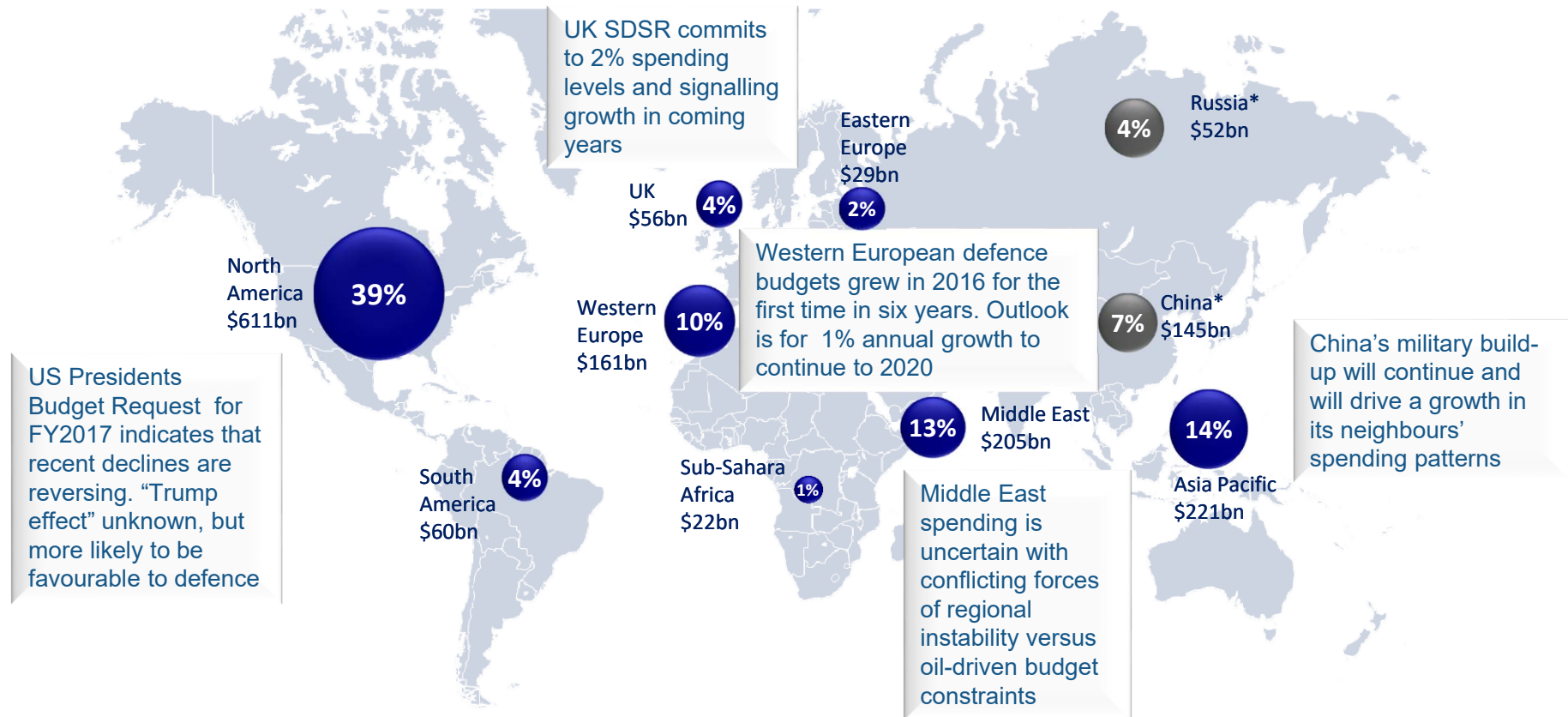
- gross debt to EBITDA	1.89x	<3.75x
- adjusted debt to EBITDA	1.89x	<3.00x
Interest cover	6.54x	>3.50x

Appendix 3. Organisation chart



Appendix 4. Market update

Global defence spending has stabilised globally, at long-term 'peace time' rate



*Total inaccessible market (Russia, China, Iran, Syria and North Korea) represents about \$200bn (13%) of global defence spend

Growth opportunities in niche market segments such as cyber defence, tactical Electronic Warfare, counter-IED and broader detection market

Appendix 5 - Glossary

APOBS	Anti-Personnel Obstacle Breaching System
CED	Chemring Energetic Devices
CHG	Chemring Group
EMD	Engineering and Manufacturing Development
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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