Chemring Group PLC

Results for the year ended 31 October 2018

Building a stronger business

Chemring Group

Carl-Peter Forster

Chairman

Safety

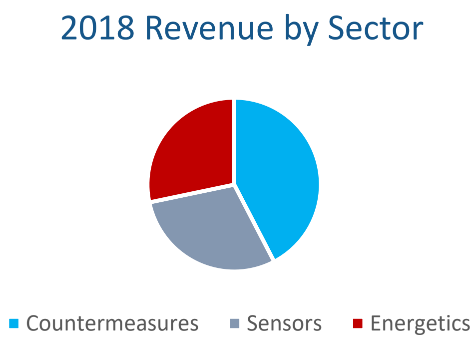
- On 10 August 2018 an incident occurred in a flare mixing building at UK Countermeasures site which resulted in the death of one colleague and serious injury to another
- The site was immediately shut down and an investigation launched into the cause
- A phased re-start of the CCM UK site started in September, with the shipping of finished goods and production of non-Energetic products

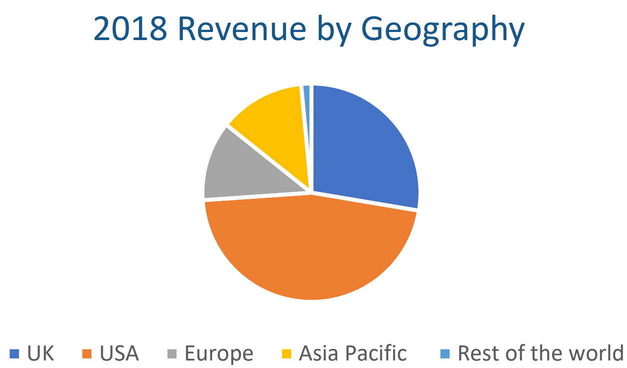
- The injured colleague continues to make good progress and we continue to support him
- The Group has taken the decision not to re-open the damaged production line; instead, it will over time transition all MTV mixing to the automated facility on site
- HSE investigation ongoing

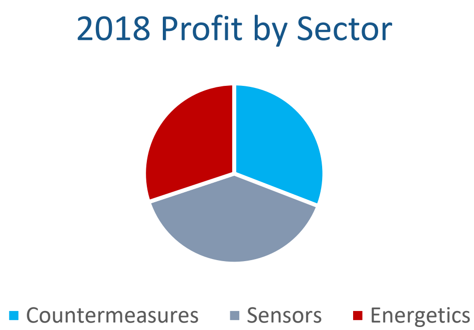
- Safety is the core value of the Company
- Commissioned a full safety review at all facilities led by Group CEO and HSE Director
- The Board remains fully committed to our goal of zero harm

Overview

- 2018 results in line with revised expectations
- Strategic decision to exit commodity Energetics businesses, resulting in an impairment charge of £69m
- Good and improving operational cash generation, offset by the impact of the incident at our UK Countermeasures site
- Good progress made on US Programs of Record and at Roke
- Non-underlying items, primarily non-cash, of £131m (FY17: £29m)
- Order book of the continuing business at year end of £394m (2017: £325m), £242m currently due as revenue in FY19, approximately 70% coverage of FY19 targeted revenue
- Board recommending a final dividend of 2.2p per ordinary share, giving a total dividend of 3.3p per ordinary share (2017: 3.0p)
- Board's expectations for the Group's FY19 performance remain unchanged, again with a significant H2 weighting







Andrew Lewis

Group Finance Director

Income statement

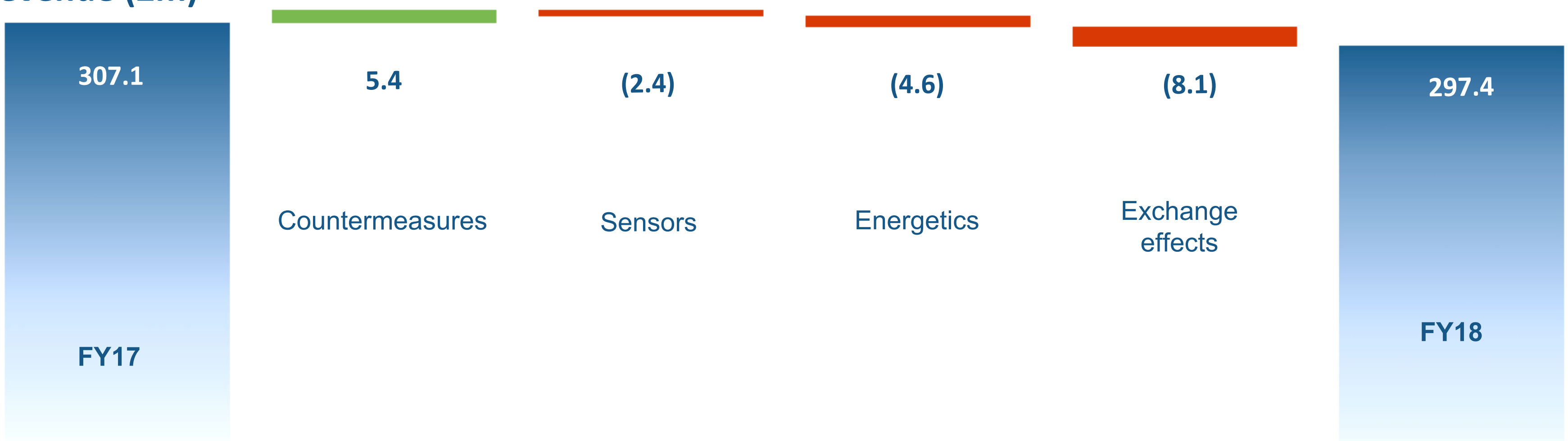
£m continuing operations		FY18	FY17
Revenue	⬇ 3%	**297.4**	307.1
Operating profit	⬇ 2%	**31.0**	31.5
Operating margin	⬆ 10bp	**10.4%**	10.3%
Finance expense	⬇ 46%	**(6.1)**	(11.3)
Profit before tax	⬆ 23%	**24.9**	20.2
Tax rate		**22.9%**	18.3%
Earnings per share		**6.9p**	5.9p
Dividend per share		**3.3p**	3.0p

- Discontinued operations revenue was £138.6m (2017: £240.4m) and operating profit £8.0m (2017: £23.9m)
- Continuing revenue and operating profit flat as impact of Salisbury incident offset progress in other areas
- Finance expense reduced following loan note repayments in November 2017 and lower intra period volatility of working capital
- The tax rate increased on FY17 due to the geographic mix of profits

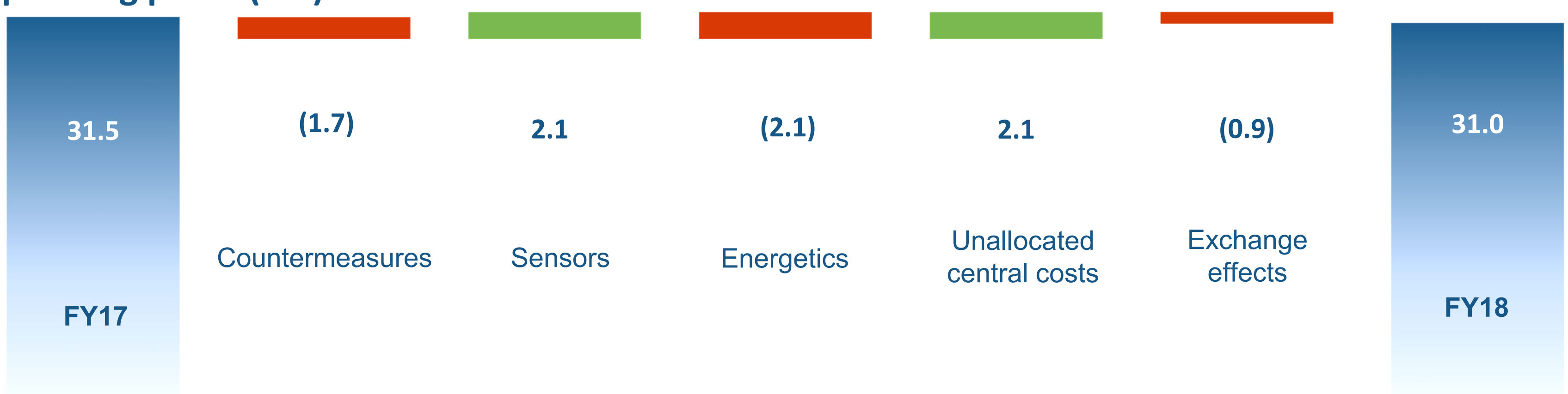
References to revenue, operating profit, profit before tax and earnings per share are to underlying measures

Revenue and profit bridges

Revenue (£m)



Operating profit (£m)

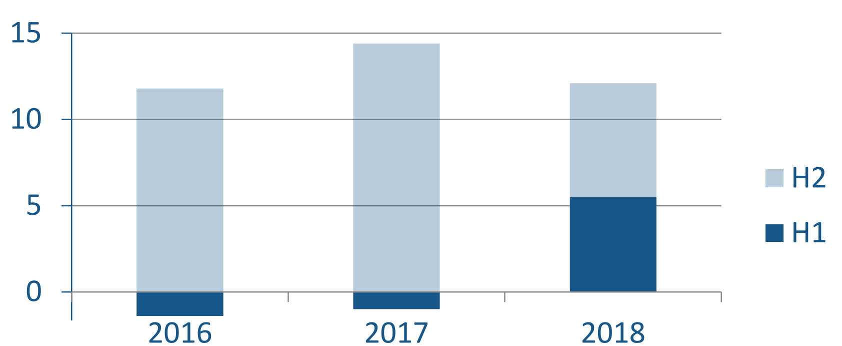


Countermeasures

		FY18 £m	FY17 £m
Revenue	↑ 1%	**126.0**	125.3
EBITDA	↓ 14%	**23.6**	27.5
EBITDA margin		**18.7%**	21.9%
Operating profit	↓ 16%	**12.1**	14.4
Operating margin		**9.6%**	11.5%
Order book		**182.8**	178.6

- H2 2018 impacted by Salisbury incident
- Strong performance in USA
- Capturing international market share through greater collaboration
- F-35 programme progressing as expected, with Australian facility closed H1 2019
- Closing order book of £183m, £116m for delivery in FY19, covering 80% of expected revenue, £92m of which can be delivered from US and Australian facilities

Operating profit (£m)

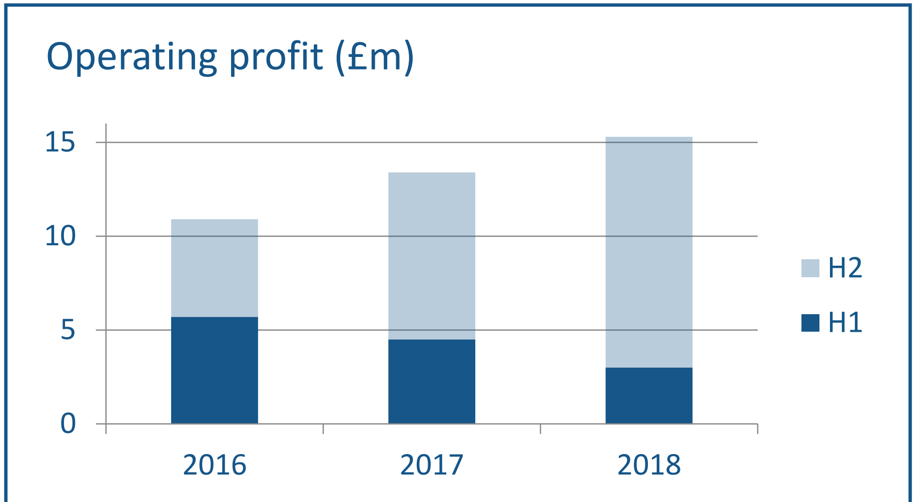


References to EBITDA, operating profit and operating margin are to underlying measures

Sensors

			FY18 £m	FY17 £m
Revenue	↓	4%	**87.3**	91.2
EBITDA	↓	4%	**18.5**	19.3
EBITDA margin			**21.2%**	21.2%
Operating profit	↑	14%	**15.3**	13.4
Operating margin			**17.5%**	14.7%
Order book			**75.4**	53.2

- Contract awards on HMDS program. Initial order partially shipped in FY18
- Chemical & Biological Detection Programs of Record – contract awards on AVCAD and EMBD; JBTDS in customer testing
- Roke had a strong year
- Closing order book of £75m, £44m for delivery in FY19, covering 40% of expected revenue



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

Sensors – Update on Programs of Record

HMDS

- Two contracts won in 2018
- $14m development contract
- $93m IDIQ, with initial delivery order of $23m
- Deliveries and further orders expected in 2019
- Program expected to be worth c.$500m over 10 years

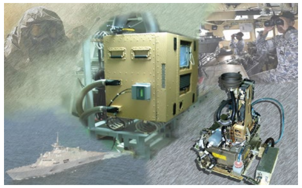
AVCAD

- Competitive bid won in 2018
- Two providers selected by customer
- $838m IDIQ contract vehicle awarded
- EMD delivery order of $4m received and this phase runs to late 2020
- DoD sourcing strategy post EMD unknown

JBTDS

- Product in customer testing for c.12–18 months
- Likely next decision point early 2020
- Program expected to be worth c.$400m over 10 years

EMBD

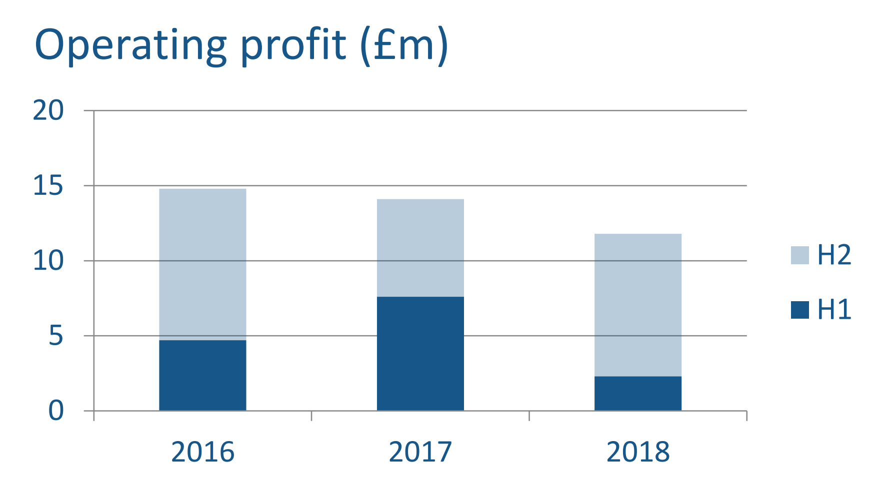


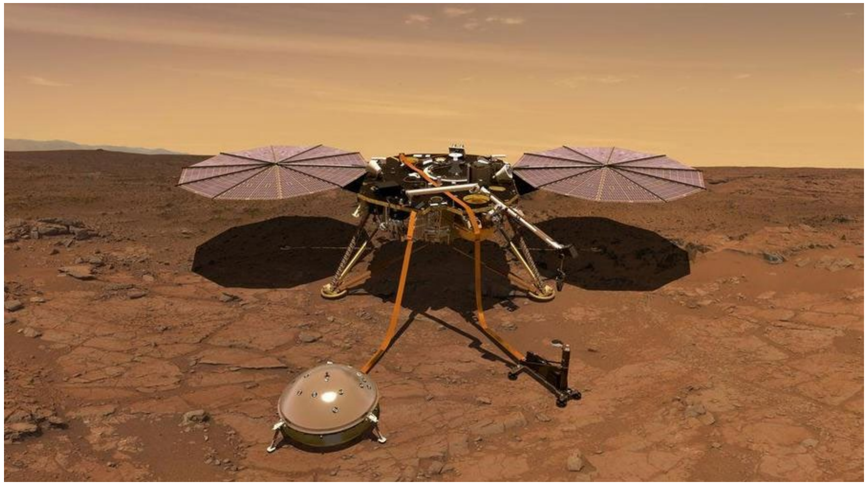
- Competitive bid won in 2018
- $24m IDIQ contract award covering EMD and LRIP
- Initial EMD delivery order of $14m
- Program expected to be worth c.$100m over 5-10 years once in LRIP

Energetics - continuing

		FY18 £m	FY17 £m
Revenue	⬇ 7%	**84.1**	90.6
EBITDA	⬇ 13%	**16.0**	18.3
EBITDA margin		**19.0%**	20.2%
Operating profit	⬇ 16%	**11.8**	14.1
Operating margin		**14.0%**	15.6%
Order book		**135.5**	93.4

- Continuing operations – a group of high quality niche businesses
- California site closure completed to plan, although some operational disruption in FY18
- Strong order intake, £124m
- Portfolio of energetic devices growing, strong long term orders at Norway and Scotland
- Closing order book of £136m, £82m for delivery in FY19, covering 87% of expected revenue



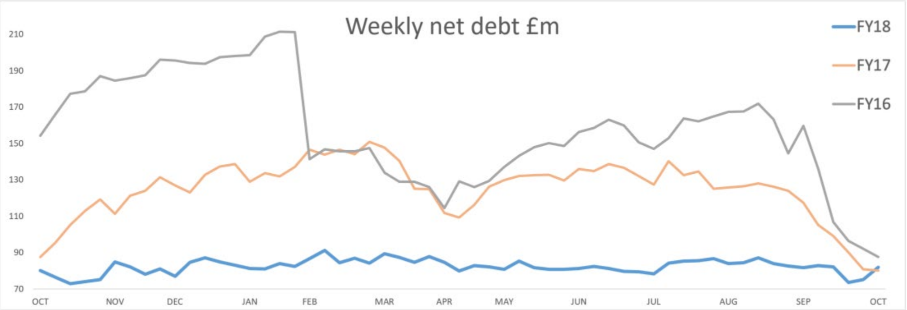


References to EBITDA, operating profit and operating margin are to underlying measures

Cash flow

£m	FY18	FY17
Cash generated from continuing underlying operations	**44.7**	41.6
Cash generated from discontinued operations	**12.2**	5.5
Cash impact of non-underlying items	**(7.6)**	(6.3)
Cash flow from operations	**49.3**	40.8
Pension scheme deficit recovery contributions	**(7.9)**	(5.0)
Tax	**(5.5)**	(3.6)
Capital expenditure	**(19.7)**	(16.5)
Dividends paid	**(8.7)**	(6.4)
Finance expense	**(6.0)**	(9.3)
Amortisation of debt finance costs	**(1.3)**	(2.4)
Foreign exchange translation	**(2.0)**	10.0
Movement in net debt	**(1.8)**	7.6
Opening net debt	**(80.0)**	(87.6)
Closing net debt	**(81.8)**	(80.0)

- Working capital down £7.9m on continuing operations, constant currency basis driven by inventory reduction
- Capex increase reflecting initial expenditure at Tennessee facility



Balance sheet

£m	FY18	FY17
Goodwill & intangibles	**146.8**	182.4
Capitalised R&D	**24.0**	33.7
Property, plant & equipment	**148.1**	160.1
Working capital	**83.7**	131.5
Net assets held for sale	**16.8**	-
Other	**(50.9)**	(25.9)
	368.5	481.8
Net debt	**(81.8)**	(80.0)
	286.7	401.8
Pension surplus / (deficit)	**7.5**	(0.6)
Net assets	**294.2**	401.2

- £98m bank facility extended to Oct 2022. £51m of PP loan notes were repaid Nov 2017, final tranche of £65m to be repaid Nov 19
- Balance sheet impairment reviews carried out in light of held for sale status and strategic product portfolio review (See Appendix 2 for detail of non-underlying impairment charge)
- Final pension deficit recovery payment made in November 2018 following April 2018 actuarial valuation
- Net debt : EBITDA (continuing) ratio of 1.64x

Carl-Peter Forster

Chairman

FY19 Outlook

- Improving outlook in global defence spending
- Order book strong; 70% of FY19 revenue covered
- Projects:
  - CCM UK re-start
  - Mobilise Programs of Record
  - Construction of Tennessee facility
  - Disposal of commoditised Energetics businesses
- Higher quality business emerging
- Board's expectations for the Group's FY19 performance remain unchanged, again with a significant H2 weighting

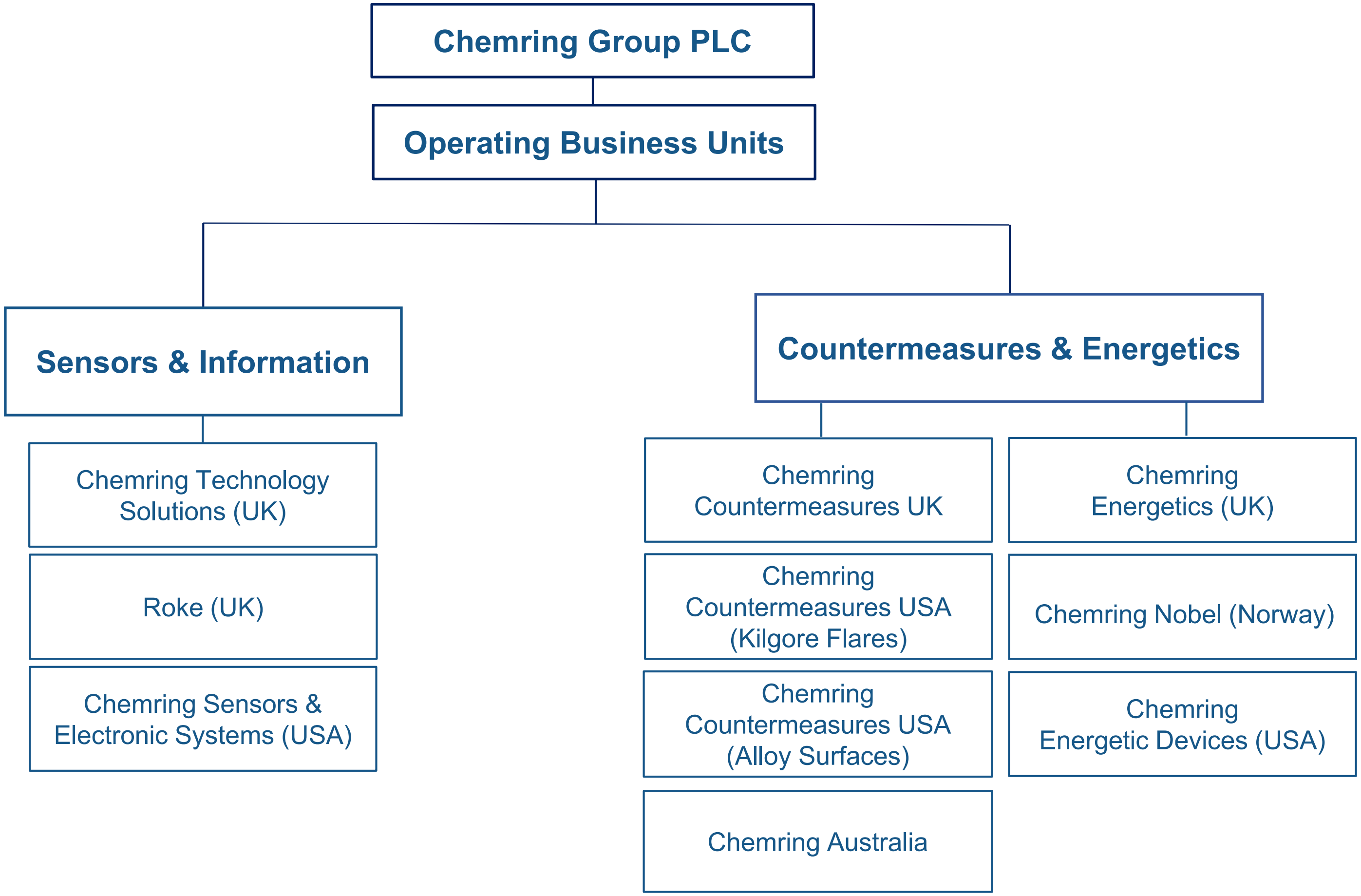
Summary

- Safety is a top priority for the Group
- Good progress made in 2018 in both financial and operational performance
- Continued progress on US Programs of Record and at Roke
- Board focused on Strategy, Structure and Culture
- Building a stronger business

Q&A

Appendices

Appendix 1. Organisation chart



Appendix 2. Non-underlying items - continuing

£m	Note	FY18 P&L cost	FY18 Cash paid
Acquired intangibles amortisation		**11.6**	**-**
Acquisition and disposal related costs	a	**4.1**	**0.3**
Business restructuring	b	**9.8**	**2.0**
Legal costs	c	**12.8**	**5.3**
Impairment of assets	d	**7.4**	**-**
Other items		**1.2**	**-**
Impact on profit before tax		**46.9**	**7.6**
US deferred tax asset write-off		**17.4**	**-**
Tax credit on non-underlying items		**(4.3)**	**-**
		60.0	**7.6**

Notes

a - Loss on disposal of Norwegian subsidiary, 3d-Radar and deferred consideration on previous acquisition

b - Transformation project at Tennessee, demolition costs and asset write off and costs of changing CEO

c - Legal costs of ongoing investigations

d – Impairment of capitalised development costs following product portfolio review

Appendix 2. Non-underlying items - discontinued

£m	Note	FY18 P&L cost	FY18 Cash paid
Acquired intangibles amortisation		**2.7**	**-**
Impairment of assets	a	**69.3**	**-**
Impact on profit before tax		**72.0**	**-**
Tax credit on non-underlying items		**(0.8)**	**-**
		71.2	**-**

Notes
a - Impairment of assets held for sale and treated as discontinued operations

Appendix 3. Impact of FX on US $ translation

Group	Constant currency movement	FY 18 restated at 2017 rates £m	FY 17 £m	FY 18 £m
Revenue	↓ 1%	**305.5**	307.1	297.4
EBITDA	↓ 6%	**51.4**	54.9	50.0
Operating profit	↑ 1%	**31.9**	31.5	31.0
Order book	↑ 19%	**387.0**	325.2	393.8

Countermeasures	Constant currency movement	FY 18 restated at 2017 rates £m	FY 17 £m	FY 18 £m
Revenue	↑ 4%	**130.7**	125.3	126.0
EBITDA	↓ 12%	**24.3**	27.5	23.6
Operating profit	↓ 12%	**12.7**	14.4	12.1
Order book	↑ 1%	**179.6**	178.6	182.8

Sensors	Constant currency movement	FY 18 restated at 2017 rates £m	FY 17 £m	FY 18 £m
Revenue	↓ 3%	**88.8**	91.2	87.3
EBITDA	↓ 3%	**18.8**	19.3	18.5
Operating profit	↑ 16%	**15.5**	13.4	15.3
Order book	↑ 39%	**73.9**	53.2	75.4

References to EBITDA and operating profit are to underlying measures

Energetics	Constant currency movement	FY 18 restated at 2017 rates £m	FY 17 £m	FY 18 £m
Revenue	↓ 5%	**86.0**	90.6	84.1
EBITDA	↓ 11%	**16.3**	18.3	16.0
Operating profit	↓ 15%	**12.0**	14.1	11.8
Order book	↑ 43%	**133.6**	93.4	135.5

Energetics continuing only

Appendix 4. Working capital

£m	**FY 18 cont**	FY17 cont	FY17 total
Inventories	**71.4**	78.0	97.6
Receivables	**45.4**	48.7	92.7
Payables	**(12.1)**	(15.8)	(37.7)
Advance receipts from customers	**(5.7)**	(10.0)	(30.7)
Advance payments to suppliers	**0.7**	0.1	25.8
Other items	**(16.0)**	(12.0)	(16.2)
	83.7	89.0	131.5

cont – refers to continuing operations not classified as held for sale in the balance sheet

Appendix 5. Modelling considerations

Financial guidance for 2019

- CapEx (inc Tennessee transformation project) - £40m-£50m
- Countermeasures site at Salisbury assumed to be operational by HY19 and contribute c£30m to FY19 revenue and breakeven after accounting for insurance proceeds and rectification costs
- Pension payments - £0.5m
- Tax rate – 23%
- Significant H2 weighting
- USD rate effect - 10¢ weaker USD reduces revenue by £20m and PBIT by £3m

Financial guidance for beyond 2019

- CapEx spend likely to stay elevated as investment in the business infrastructure continues
- Pension payments - £nil
- Interest payments likely to reduce in 2020 following repayment of final Private Placement Loan Notes in November 2019
- Increased investment in resources to improve governance, manage risk and invest in growth opportunities

Appendix 6. Glossary

Acronym	Meaning	Acronym	Meaning
AGPR	Advanced Ground Penetrating Radar	**IDIQ**	Indefinite Delivery Indefinite Quantity
APAC	Asia Pacific Region	**IED**	Improvised Explosive Device
AVCAD	Aerosol & Vapor Chemical Agent Detector	**JBTDS**	Joint Biological Tactical Detection System
CED	Chemring Energetic Devices	**LRIP**	Low Rate Initial Production
CHA	Chemring Australia	**LTI**	Lost Time Incident
CHG	Chemring Group	**MJU**	Multi Jettison Unit
CM	Countermeasures	**MTV**	Magnesium Teflon Viton
EMBD	Enhanced Maritime Biological Detection	**NGCD**	Next Generation Chemical Detector
EMD	Engineering and Manufacturing Development	**NSA**	Non-Standard Ammunition
EW	Electronic Warfare	**POR**	Program of Record
F-35	F-35 Joint Strike Fighter	**PP**	Private Placement
FRP	Full Rate Production	**SMD**	Special Material Decoy
HMDS	Husky Mounted Detection System	**US DoD**	United States Department of Defense

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