Financial overview

	Half year to 30 June	
	2016 **£m**	2015 £m
Revenue	**291.0**	299.8
Headline operating profit	**49.3**	54.1
Amortisation of acquired intangible fixed assets	**(2.2)**	(2.1)
Operating profit prior to exceptional items	**47.1**	52.0
Reorganisation costs	**–**	(19.9)
Operating profit	**47.1**	32.1

Revenue for the half year was £291.0m (2015: £299.8m), a decrease of 2.9% compared to the same period last year. At constant exchange rates, revenue decreased 8.1% (£24.2m). Favourable foreign exchange rate movements resulted in a £15.4m positive effect.

Headline operating profit decreased to £49.3m (2015: £54.1m) and headline operating margin decreased to 16.9% (2015: 18.0%). At constant exchange rates, headline operating profit decreased £8.2m.

The amortisation of acquired intangible assets arises from acquisitions in prior years. The charge has increased to £2.2m (2015: £2.1m).

Operating profit increased to £47.1m (2015: £32.1m) and operating margin was 16.2% (2015: 10.7%). In 2015, operating profit was impacted by exceptional reorganisation costs of £19.9m.

Exceptional costs

There were no exceptional costs in the first six months of 2016 (2015: £19.9m). The 2015 charge comprised reorganisation costs relating to the exit from Brazil and restructuring initiatives across the Group.

Profit before taxation

	Half year to 30 June	
	2016 **£m**	2015 £m
Headline operating profit	**49.3**	54.1
Net finance charge	**(1.2)**	(1.5)
Headline profit before taxation	**48.1**	52.6
Amortisation of acquired intangible fixed assets	**(2.2)**	(2.1)
Headline profit before taxation prior to exceptional items	**45.9**	50.5
Reorganisation costs	**–**	(19.9)
Profit before taxation	**45.9**	30.6

Finance charge

The net finance charge for the Group was £1.2m compared to £1.5m in 2015.

	Half year to 30 June	
	2016 **£m**	2015 £m
Net interest payable	**–**	0.1
Financing costs	**0.7**	0.8
Bank and other charges	**0.3**	0.4
Pension finance charge	**0.2**	0.2
Net finance charge	**1.2**	1.5

Cash flow

	Half year to 30 June	
	2016 **£m**	2015 £m
Headline operating profit	**49.3**	54.1
Add back non-cash items:		
Depreciation and amortisation	**25.9**	25.4
Impairment of fixed assets	**0.2**	–
Share-based payments	**1.6**	0.8
(Profit) / loss on disposal of property, plant and equipment	**(0.1)**	0.6
Headline EBITDA[1]	**76.9**	80.9
Net capital expenditure	**(31.0)**	(29.2)
Net working capital movement	**(7.9)**	(11.5)
Headline operating cash flow	**38.0**	40.2
Cash cost of restructuring	**(4.3)**	(3.5)
Operating cash flow	**33.7**	36.7
Interest	**(0.9)**	(1.2)
Taxation	**(11.9)**	(14.9)
Free cash flow	**20.9**	20.6

Free cash flow for the period was £20.9m compared to £20.6m in the first six months of 2015. The decrease in headline EBITDA was offset by lower net working capital cash outflows and lower tax payments.

The net working capital outflow for the six month period amounted to £7.9m (2015: £11.5m). Receivables increased £3.6m (2015: £6.7m) as a result of the normal seasonally higher revenues in May and June in comparison to November and December. Receivable days at 30 June 2016 are 63 days (31 December 2015: 63 days and 30 June 2015: 61 days). Payables decreased £6.3m (2015: £5.6m) and inventory decreased £2.2m (2015: £0.9m).

The utilisation of restructuring provisions resulted in a cash outflow of £4.3m (2015: £3.5m).

The Group continued to manage carefully its capital expenditure programme and is focused on growing the Group's Specialist Technology offerings and expanding capacity in emerging markets. Net capital expenditure for the first half was £31.0m (2015: £29.2m) and the ratio to depreciation was 1.2 times (2015: 1.1 times). Major capital projects that were in progress during the first half of 2016 included expansion of our production facilities in Mexico, increased aerospace capacity in USA and France and ongoing expansion of our Specialist Technologies capability. Central expenditure has also continued on the implementation of new ERP and HR systems.

Income taxes paid during the first six months at £11.9m were £3.0m lower than the same period last year, reflecting the timing of payments made in various tax jurisdictions.

Taxation

The tax charge in the first half of 2016 was £12.6m, compared to a charge of £10.4m for the same period of 2015. The effective tax rate of 27.5% (2015: 34.1%) results from the impact of differing tax rates in each of the numerous jurisdictions in which the Group operates. In 2015, the effective tax rate of 34.1% was impacted by the phasing of the reorganisation costs, particularly in respect of Brazil, which did not give rise to a corresponding tax credit in the territories to which they related.

The headline tax rate, excluding the impact of reorganisation costs, is 27.5% in the first six months of 2016 (2015: 23.7%). The Group expects that this headline tax rate will not differ significantly in the second half of 2016.

1 Earnings before interest, tax, depreciation, amortisation, impairment, profit or loss on disposal of property, plant and equipment and share-based payments.

Earnings per share
Basic headline earnings per share from operations for the half year were 18.3p (2015: 21.1p). Basic earnings per share from operations for the half year were 17.5p (2015: 10.6p). Diluted earnings per share were 17.5p (2015: 10.6p).

Dividend
The Board has declared an interim dividend of 5.0p (2015: 4.8p) which represents an increase of 4.2% over the prior year. The interim dividend will be paid on 4 November 2016 to all shareholders on the register at the close of business on 7 October 2016.

Net debt
Group net debt at 30 June 2016 was £5.5m (31 December 2015 net cash: £12.3m and 30 June 2015 net debt: £7.0m). Loans and letters of credit drawn under the committed facilities at 30 June 2016 totalled £7.4m, compared to £1.8m at 31 December 2015 and £13.8m at 30 June 2015. The Group continues to be able to borrow at competitive rates and therefore currently deems this to be the most effective means of funding.

Borrowing facilities
The Group is financed by a mix of cash flows from operations, short-term borrowings, longer-term loans and finance leases. The Group's funding policy aims to ensure continuity of finance at reasonable cost, based on committed and uncommitted facilities and loans from several sources over a spread of maturities. At 30 June 2016, the Group had the following committed facilities:

Facility	Expiry date	Facility £m	Loan and letter of credit utilisation £m	**Facility headroom £m**
£230m Revolving Credit	3 July 2019	230.0	5.4	**224.6**
$10m Letter of Credit	31 August 2016	7.5	2.0	**5.5**
		237.5	7.4	**230.1**

Defined benefit pension schemes
The Group's principal defined benefit pension obligations have been reviewed as at 30 June 2016. The surplus in the UK scheme is £1.0m (31 December 2015: £2.7m deficit). In France, the deficit in relation to the primarily unfunded cash lump sum obligation is £9.7m (31 December 2015: £8.6m). The sum of the deficits for all other Group schemes is £7.5m (31 December 2015: £6.6m). These amounts are fully provided at 30 June 2016. The principal actuarial assumptions are unchanged from those used as at 31 December 2015.

Principal risks and uncertainties
The directors have reconsidered the principal risks and uncertainties of the Group. The result of the referendum on the future of the UK's membership in the European Union is not expected to have a material transactional impact as customers are served locally and cross-border trading is minimal. The risk of a wider macro-economic effect as a result of the UK leaving the EU is addressed by the Group's existing Markets risk. Accordingly, the directors do not consider that the principal risks and uncertainties of the Group have significantly changed since the publication of the Annual Report for the year ended 31 December 2015. The risks and associated risk management processes can be found on pages 24, 25, 26, 110 and 111 of the 2015 Annual Report, which is available at www.bodycote.com. The risks referred to and which could have a material impact on the Group's performance for the remainder of the current financial year relate to:

- Markets;
- Loss of key customers;
- Competitor action;
- Safety and health;
- Service quality;
- Major disruption at a facility;
- Information technology projects;
- Regulatory and legislative compliance;
- Liquidity;
- Interest rate fluctuation; and
- Currency exchange rate fluctuation.

Going concern
As stated in note 1 to the condensed financial statements, the directors have formed a judgement, at the time of approving the condensed financial statements, that there is a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason the directors continue to adopt the going concern basis in preparing the condensed financial statements.

Summary and outlook
The Group has again demonstrated its ability to deal with challenging market conditions, including delivery of a continued improvement in the AGI margin. This has been achieved against a background of subdued demand for industrial machinery and a further substantial decline in oil & gas revenues.

Looking ahead, and noting the Group's lack of visibility, we expect growth in our aerospace and automotive markets to continue and the sequential decline in oil & gas activity to have largely abated. Recent demand in general industrial markets has been softer than expected and improvements are not anticipated in the second half. However, if current exchange rates prevail, we expect weakness in overall trading, for the year as a whole, to be offset by the benefit of currency translation.

The Group continues to benefit from the flexibility afforded by the strength of its balance sheet, with minimal leverage and continuing strong cash generation.

We will continue to follow our strategy of investing in areas of robust profit opportunity, notably in Specialist Technologies, and in further enriching the mix towards higher added value services in Classical Heat Treatment.

S.C. Harris
Group Chief Executive
28 July 2016

D.F. Landless
Group Finance Director
28 July 2016