Interim management report continued

Financial Overview

Revenue and headline operating profit

	Revenue 2013 £m	Revenue 2012 £m	Headline operating profit 2013 £m	Headline operating profit 2012 (Restated) £m	Headline operating margin 2013 %	Headline operating margin 2012 (Restated) %
ADE	**133.8**	130.3	**34.5**	31.3	**25.8**	24.0
AGI	**182.7**	171.0	**25.1**	22.8	**13.7**	13.3
	316.5	301.3	**59.6**	54.1	**18.8**	18.0
Head office costs	**–**	–	**(7.2)**	(6.8)	**–**	–
Total	**316.5**	301.3	**52.4**	47.3	**16.6**	15.7

Half year to 30 June

Revenue for the half year was £316.5m (2012: £301.3m), an increase of 5.0% compared to the same period last year. In constant currencies the increase was 2.6% (£7.7m), of which £21.2m (7.0%) came from acquisitions, all of which were completed in 2012, together with a like-for-like reduction in revenue of £13.5m (4.5%). There was a year-on-year exchange gain of £7.5m.

Headline operating profit increased to £52.4m (2012: £47.3m) and headline operating margin improved to 16.6% (2012: 15.7%). The contribution to headline operating profit from acquisitions was £4.6m and the impact of exchange was a benefit of £1.7m, which offset a like-for-like reduction in headline operating profit of £1.2m. Operating profit increased to £50.3m (2012: £45.4m) and operating margin was 15.9% (2012: 15.1%).

Headline operating margins for the first six months improved in both ADE and AGI. ADE reported a headline operating margin of 25.8% (2012: 24.0%) and AGI reported a headline operating margin of 13.7% (2012: 13.3%).

Profit before taxation

Half year to 30 June	2013 £m	2012 (Restated) £m
Headline operating profit	**52.4**	47.3
Net finance charge	**(1.8)**	(1.5)
Headline profit before taxation	**50.6**	45.8
Amortisation of acquired intangible fixed assets	**(2.1)**	(0.7)
Acquisition costs	**–**	(1.2)
Profit before taxation	**48.5**	43.9

Finance charge

The net finance charge for the Group was £1.8m compared to £1.5m in 2012. Of the increase, £0.3m relates to higher average net debt, as a result of the 2012 acquisitions, offset by a reduction of £0.1m due to lower interest rates. Higher financing costs of £0.1m result primarily from the refinanced €125m Revolving Credit Facility completed earlier in the year.

Half year to 30 June	2013 £m	2012 (Restated) £m
Net interest payable	**0.4**	0.2
Financing costs	**0.7**	0.6
Other charges	**0.4**	0.4
Pension finance charge[1]	**0.3**	0.3
Net finance charge	**1.8**	1.5

Exceptional costs

Exceptional costs for the first six months amounted to £2.1m (2012: £1.9m). The charge comprises amortisation of acquired intangible fixed assets of £2.1m (2012: £0.7m) and acquisition costs of £nil (2012: £1.2m).

Cash flow

Half year to 30 June	2013 £m	2012 (Restated) £m
Headline operating profit	**52.4**	47.3
Add back non-cash items:		
Depreciation and amortisation	**28.2**	25.1
Share-based payments	**3.0**	3.0
Headline EBITDA[2]	**83.6**	75.4
Net capital expenditure	**(28.6)**	(26.6)
Net working capital movement	**(8.5)**	3.5
Headline operating cash flow	**46.5**	52.3
Cash cost of restructuring	**(3.0)**	(2.0)
Acquisition costs	**–**	(1.2)
Operating cash flow	**43.5**	49.1
Interest	**(1.7)**	(1.2)
Taxation	**(14.3)**	(9.0)
Free cash flow	**27.5**	38.9

Free cash flow for the period was £27.5m compared to £38.9m in the first six months of 2012. The reason for the decrease compared to 2012 is primarily a result of the working capital outflow in the period, and an increase in taxes paid.

The net working capital outflow for the six month period amounted to £8.5m (2012: inflow of £3.5m). Inventories increased by £0.3m (2012: £0.4m increase). Receivables increased by £12.8m (2012: £7.9m increase) as a result of the seasonally higher sales in May and June in comparison to November and December and the impact of 30 June falling at a weekend pushing some cash receipts into July. Debtor days outstanding at 30 June 2013 remained consistent with 30 June 2012 at 59 days (31 December 2012: 58 days). Payables increased by £4.4m (2012: £11.9m increase). The movement in payables in 2012 was impacted by the timing of significant capital expenditure payments.

Provision balances decreased by £2.8m over the period (2012: £2.5m decrease), predominantly reflecting cash expenditure on restructuring.

1 Restated for the adoption of IAS 19 (Revised) 'Employee Benefits', which has the effect of reducing the pension finance charge by £0.3m.
2 Earnings before interest, tax, depreciation, amortisation, impairment, gain or loss on disposal of property, plant and equipment, cash flow relating to restructuring, acquisition costs and share-based payments.

The Group has continued to manage its capital expenditure programme carefully. Net capital expenditure for the first half was £28.6m (2012: £26.6m) and the ratio to depreciation was 1.0 times (2012: 1.1 times). Major capital projects that were in progress during the first half of 2013 included additional investment in the HIP business in the USA, the S³P business in Europe and additions to heat treatment capacity in both Europe and the USA.

Income taxes paid during the first six months at £14.3m were £5.3m higher than in 2012, reflecting the increase in profits generated in 2013 compared to the first half of 2012, aided by the impact of acquisitions made in the second half of 2012. Additionally, tax losses in certain countries were fully accessed and exhausted in 2012, resulting in higher cash tax payments for the subsequent comparative period.

Taxation

The tax charge in the first half of 2013 was £12.5m, compared to a charge of £11.2m for the same period of 2012. The effective tax rate of 25.7% (2012: 25.3%) results from the impact of differing tax rates in each of the numerous jurisdictions in which the Group operates. The rate represents the weighted average of corporation taxes expected for the full financial year.

Earnings per share

Basic headline earnings per share from operations for the half year were 20.0p (2012: 18.3p). Basic earnings per share from operations for the half year were 18.9p (2012: 17.3p). Diluted earnings per share were 18.9p (2012: 17.3p).

Dividend

The Board has declared an interim dividend of 4.4p (2012: 4.0p) which represents an increase of 10% over the prior year. The interim dividend will be paid on 7 November 2013 to all shareholders on the register at the close of business on 4 October 2013.

Net debt

Group net debt at 30 June 2013 was £27.1m (30 June 2012: £16.7m and 31 December 2012: £34.2m). Loans and letters of credit drawn under the committed facilities at 30 June 2013 totalled £22.6m, compared to £38.4m at 31 December 2012 and £22.2m at 30 June 2012. The Group continues to be able to borrow at competitive rates and therefore currently deems this to be the most effective means of funding. The debt to equity ratio at 30 June 2013 was 5% (2012: 3%).

Liquidity and investments

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 facilities from several sources over a spread of maturities. At 30 June 2013, the Group had the following committed facilities:

Facility	Expiry date	Facility £m	Loan and Letter of Credit Utilisation £m	Facility Headroom £m
£125m Revolving Credit	31 August 2016	125.0	17.4	**107.6**
€125m Revolving Credit	1 March 2018	107.1	–	**107.1**
		232.1	17.4	**214.7**
$10m Letter of Credit	31 August 2016	6.6	5.2	**1.4**
		238.7	22.6	**216.1**

Defined benefit pension schemes

The Group's principal defined benefit pension obligations have been reviewed as at 30 June 2013. The IAS 19 (Revised) deficit in the UK scheme decreased to £3.9m (31 December 2012: £4.2m). The decrease is a result of the contributions paid, which exceeded the interest on the deficit. In France, for its primarily unfunded cash lump sum obligation, the deficit is £8.7m (31 December 2012: £8.0m). The sum of the deficits for all other Group schemes is £7.2m (31 December 2012: £6.8m).

For the year ended 31 December 2013 the Group is required to adopt IAS 19 (Revised) 'Employee Benefits'. The accounts have been restated and the impact of the restatement is set out in note 1.

Acquisitions

In accordance with IFRS 3 'Business Combinations' the Group has carried out a review of the provisional acquisition fair values recognised in the accounts at 31 December 2012. Adjustments made to provisional acquisition fair values as a result of this review are not considered material to the financial statements.

Summary and outlook

The Group delivered a good first half result, with last year's acquisitions performing well. Improvements in mix and rigorous cost control outweighed softness in demand, resulting in increased margins.

Looking forward, we expect a broadly similar outcome in the second half and therefore the Board continues to expect modest progress for the year as a whole.

The Board remains confident that Bodycote's strategy will continue to deliver good profits, cash and returns through the business cycle.

S.C. Harris
Group Chief Executive
25 July 2013

D.F. Landless
Group Finance Director
25 July 2013