



annual report 2018

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 For the online version of this report go to [bodycote.annualreport2018.com](http://bodycote.annualreport2018.com)

## At a glance

Operating an international network of facilities, Bodycote is the world's leading provider of thermal processing services.

Experienced in supporting large multinational customers and their supply chains, as well as local niche specialists, Bodycote provides a vital link in the manufacturing process for virtually every market sector including aerospace and defence, automotive, power generation, oil & gas, and general industrial.

### The core values underpinning everything we do Honesty and Transparency

We are honest and act with integrity. This is not something we take for granted. Bodycote lives by a culture of honest and transparent behaviour, which is at the core of all our business relationships.

### Respect and Responsibility

We manage our business with respect, applying an ethical approach to our dealings with those we interact with. We believe in taking ownership, and being mindful of the impact of our actions.

### Creating Value




Creating value is the very essence of our business and needs to be the focus of our endeavours. We create value for our customers, our employees and our shareholders.

Throughout this report you will see illustrations which link our business and strategy:

#### Strategy & Core Values

- |   |   |
|---|---|
|  Aerospace, Defence & Energy |  Automotive & General Industrial |
|  Rapid growth countries      |  Technology                      |
|  Customer service            |  Core values                     |

#### Key Performance Indicators

- |  |   |
|--|---|
|  Return on capital employed |  Headline earnings per share |
|  Return on sales            |  Free cash flow              |
|  Accident frequency         |  Carbon footprint            |

## Our technologies

### Classical Heat Treatments

Bodycote's Classical Heat Treatments describe a group of mature heat treatment processes and include metal joining technologies which are used to join and assemble parts.

### Specialist Technologies

Our Specialist Technologies are a group of early phase proprietary technologies which require specialist expertise and technology and where we are the only provider of, or one of the leading providers. These processes enable our customers to produce unique high value adding products.

## Our markets

### 1. Aerospace and Defence

Largely focused on civil aerospace, we primarily treat engine, landing gear and airframe components to improve performance.

### 2. Energy

Primarily extending the life of products used in the onshore, offshore and subsea oil & gas industry, largely in North America and Western Europe.

### 3. Automotive

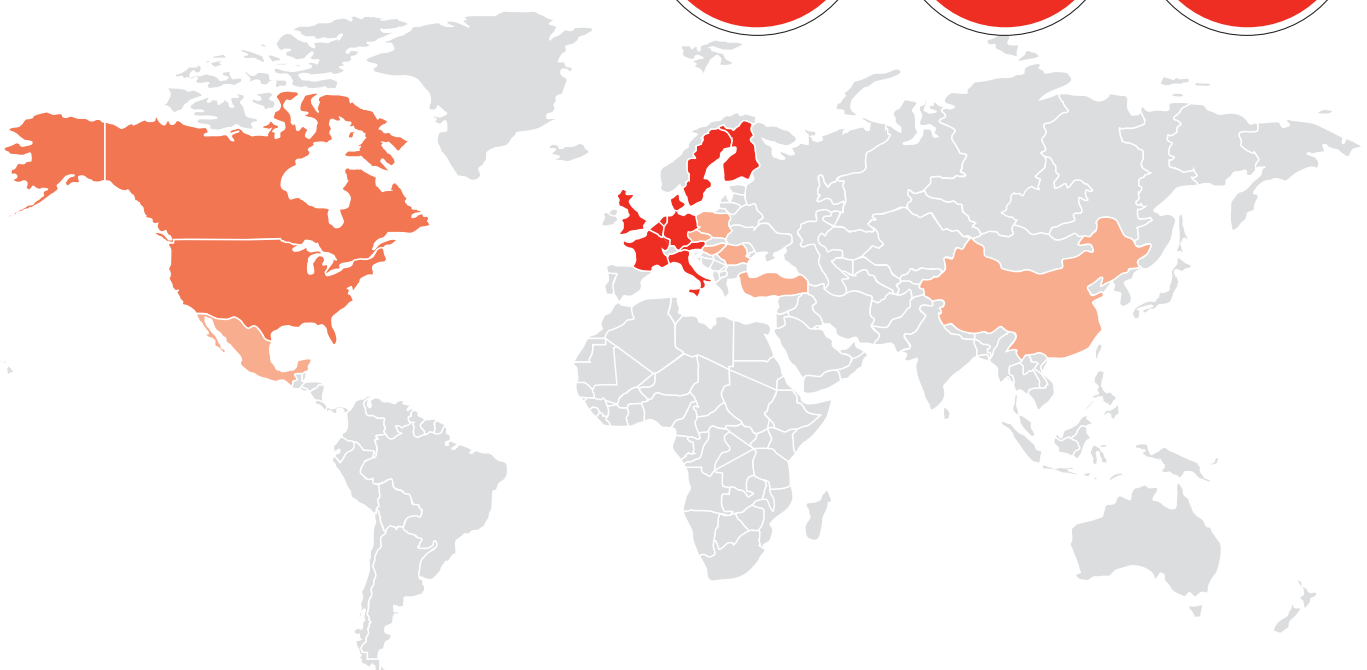
Focused on the car and light truck market, heat treatment delivers greater strength and durability for key components.

### 4. General Industrial

We serve a very broad range of customers across our general industrial facilities. These customers range from industrial machinery to tooling, construction, electronics and medical equipment.

## Where we operate

- Western Europe
- North America
- Emerging Markets



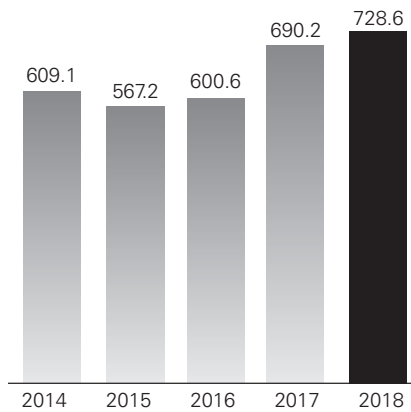
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# Highlights

## Financial Highlights

### Revenue

£m

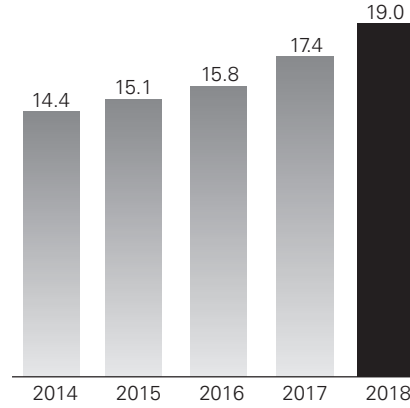


**£728.6m**

+5.6%

### Dividend per share

pence

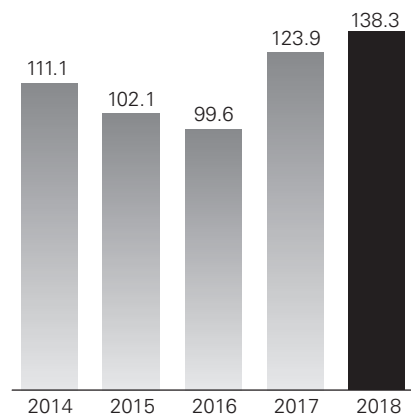


**19.0p**

+9.2%

### Headline operating profit

£m

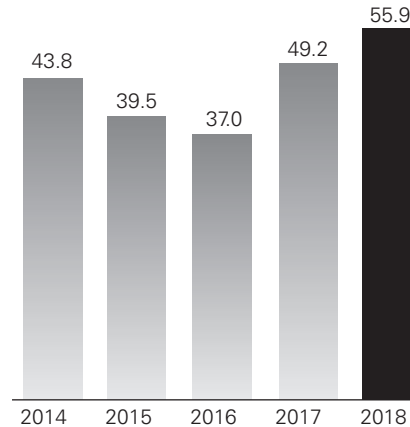


**£138.3m**

+11.6%

### Headline earnings per share

pence

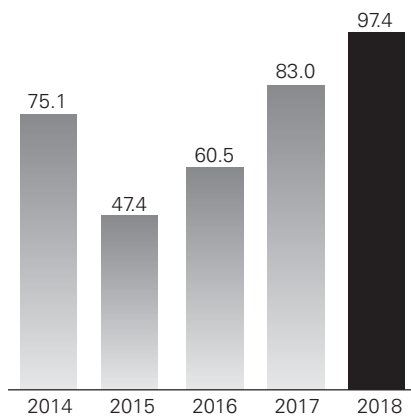


**55.9p**

+13.6%

### Free cash flow

£m

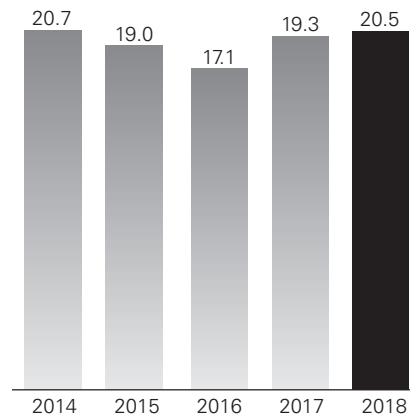


**£97.4m**

17.3%

### Return on capital employed

%



**20.5p**

+6.2%

# Financial highlights

	2018	2017	% change	% change at constant currency
Revenue	<b>£728.6m</b>	£690.2m	5.6%	6.7%
Headline operating profit <sup>1</sup>	<b>£138.3m</b>	£123.9m	12%	13%
Return on sales <sup>1</sup>	<b>19.0%</b>	18.0%		
Headline profit before taxation <sup>1</sup>	<b>£136.4m</b>	£121.5m	12%	13%
Free cash flow <sup>1</sup>	<b>£97.4m</b>	£83.0m	17%	
Basic headline earnings per share <sup>2</sup>	<b>55.9p</b>	49.2p	14%	
Ordinary dividend per share	<b>19.0p</b>	17.4p	9%	
Special dividend per share	<b>20.0p</b>	25.0p		
Return on capital employed <sup>1</sup>	<b>20.5%</b>	19.3%		

## Statutory results

	2018	2017
Operating profit	<b>£134.1m</b>	£119.4m
Profit before taxation	<b>£132.2m</b>	£117.0m
Basic earnings per share	<b>54.2p</b>	51.0p

## Operational highlights

- Revenue growth of 6.7% at constant currency
  - Specialist Technologies delivered double digit growth of 12%
  - Emerging Markets growth of 21%
  - Civil aviation revenues up 8%
- 12% growth in headline operating profit to £138.3m
- Return on sales improvement to 19.0% (2017: 18.0%)
- ROCE<sup>1</sup> increased to 20.5% (2017: 19.3%)
- Free cash flow of £97.4m (2017: £83.0m), after expansionary capex of £44.1m
- Headline operating cash conversion at 93%<sup>1</sup>
- Full year ordinary dividend 19.0p, up 9%
- Special dividend of 20.0p

1. The headline performance measures represent the statutory results excluding certain non operational items. These are deemed alternative performance measures under the European Securities and Markets Authority guidelines. Please refer to note 1 to the financial statements on page 98 for a reconciliation to the IFRS equivalent.

2. A detailed EPS reconciliation is provided in note 8 on page 108.

# Strategic report

The Group **Strategic report** provides a review of the business for the financial year and describes how we manage risks.

The report outlines the developments and performance of the Group during the financial year, the position at the end of the year and discusses the main trends and factors that could affect the future.

Key performance indicators are published to show the performance and position of the Group. Page 8 outlines the Group's strategy and objectives, along with the business model on page 9.

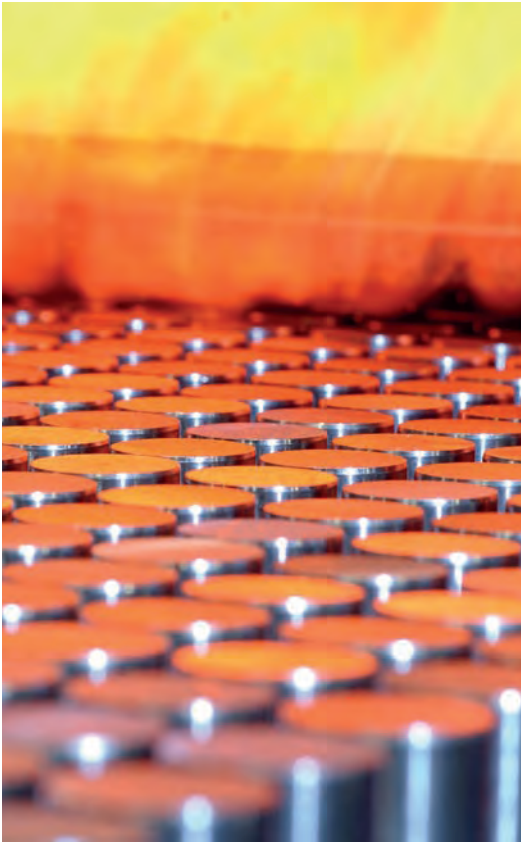
The directors, in preparing this Strategic report, have complied with s414C of the Companies Act 2006.

This Strategic report has been prepared for the Group as a whole and therefore gives greater emphasis to those matters which are significant to Bodycote plc and its subsidiary undertakings when viewed as a whole.

## The Strategic report discusses the following areas:

- Our technologies
- Global network
- Strategy and objectives
- Our business model
- Our stakeholders
- Measuring progress
- Chair's statement
- Chief Executive's review
- Business review – The ADE Business
- Business review – The AGI Business
- Chief Financial Officer's report
- Principal risks and uncertainties
- Corporate responsibility and sustainability

# Our technologies



## Classical Heat Treatment

Classical Heat Treatment is the controlled heating and cooling process of metals in order to obtain the desired mechanical, chemical and metallurgical properties during the manufacturing of a product.

It provides wear resistance, strength or toughness depending on the application. Surface hardness can be controlled by diffusing elements such as carbon and nitrogen into the metal during the heating stages of the process. Classical Heat Treatment is an indispensable set of processes within the manufacturing chain of most of the products used in life. A seat belt buckle for example, hardens after heat treatment so that it keeps the passenger safe during an accident. A screwdriver lasts longer without wear or a screw fastens components together without fail only after heat treatment.

Classical Heat Treatment is carried out in precisely controlled industrial furnaces which can heat up to temperatures above 1000C and use quenchants like oil, water or Nitrogen gas to cool the heated material. During the process the microstructure of the metal transforms into a different structure which results in hardening or softening of the material depending on the process. Engineers can design thinner, lighter but stronger components with the help of Classical Heat Treatment.



## Specialist Technologies

A selection of highly differentiated, early stage processes with high margins, large market opportunity and good growth prospects. Bodycote is either the clear market leader or one of the top players among few competitors

### Hot Isostatic Pressing (HIP Services)

Improves component integrity and strength by application of extreme pressure & heat

### HIP PF inc. Powdermet®

Additive manufacturing of often complex components in conjunction with HIP

### Specialty Stainless Steel (S<sup>3</sup>P)

Improves the strength, hardness and wear resistance of stainless steels

### Surface Technology

Enhances component life using ceramic and metal coatings

### Low Pressure Carburising (LPC)

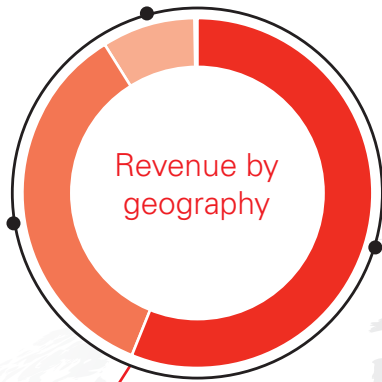
Provides a hardened surface and tough core in a "clean" process under vacuum

### CiD®

Improves corrosion resistance & wear properties without use of chrome

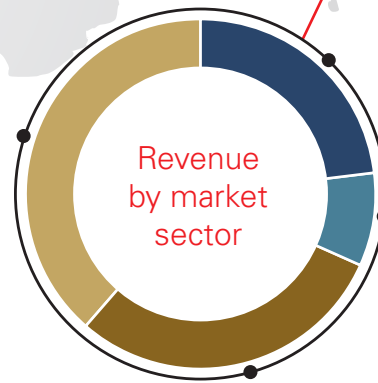
# Global network

Bodycote is experienced in all major market sectors and is able to combine the capability and expertise of a network of more than 180 facilities to deliver global or local services for customers.



Group revenue by market sector – £m

Aerospace and Defence	168.5
Energy	62.5
Automotive	216.3
General Industrial	281.3
<b>Total</b>	<b>728.6</b>



Group revenue by geography – £m

Western Europe	409.7
North America	255.6
Emerging markets	63.3
<b>Total</b>	<b>728.6</b>

## Overview

As the only global provider of subcontract thermal processing services, Bodycote is able to offer significant advantages to its customers. Through an international network of facilities, Bodycote can effectively utilise a wealth of knowledge, experience and specialist expertise to deliver quality service when and where it is needed.

The network operates from more than 180 facilities, with customers able to benefit from Bodycote's comprehensive range of services from multiple locations. Customers know that if their business expands, Bodycote will have the capability to meet their needs. They recognise that if they were to broaden their manufacturing footprint, Bodycote would be able to assist them. They are aware that they can obtain the same process to the same quality standards from multiple locations.

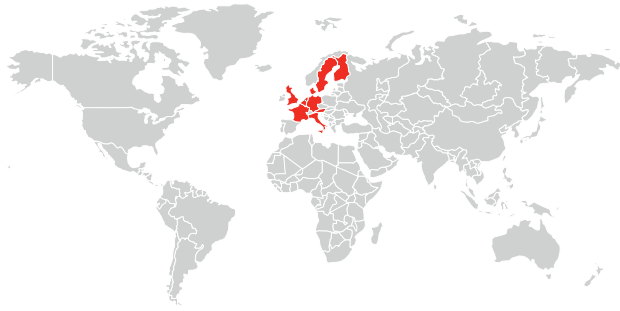
Such a large network brings economies of scale, with technology developed at one location being available globally if the market requires it. Similarly, network utilisation is enhanced by using logistics to put customers' work into the most effective facilities to meet their requirements.

The Bodycote network has a wealth of technical accreditations, some industry or customer specific, others more general. Individual operations concentrate on the accreditations suited to their market.

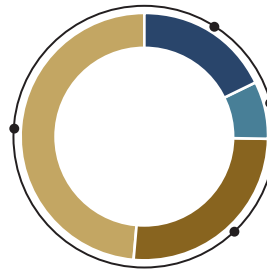


Although Bodycote is a UK company, 92% of the Group’s revenue is derived outside the UK. With facilities in 23 countries, Bodycote is truly global.

### Western Europe



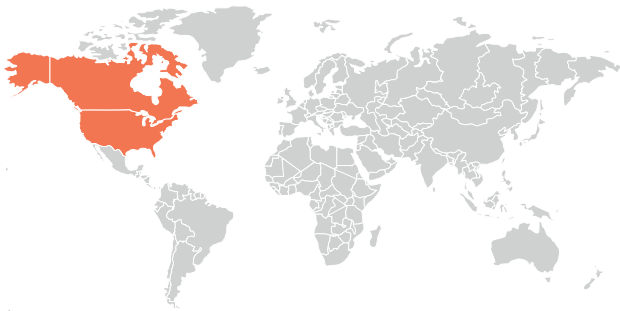
Bodycote operates more than 100 facilities in Western Europe and is the number one provider of thermal processing services, with by far the largest network and a comprehensive service offering.



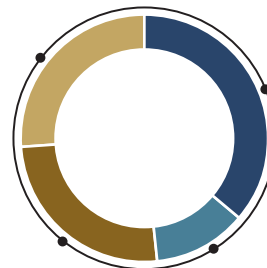
#### Revenue by market sector – £m Western Europe

Aerospace and Defence	73.5
Energy	31.2
Automotive	106.8
General Industrial	198.2
<b>Total</b>	<b>409.7</b>

### North America



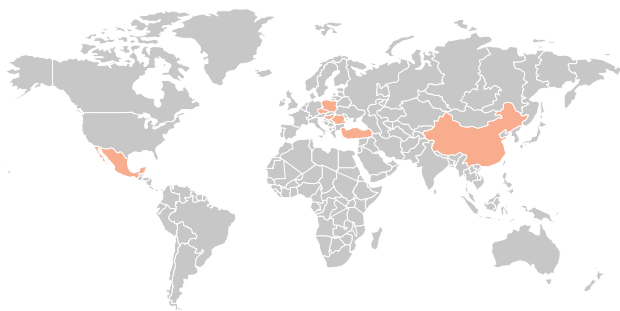
Bodycote is the largest provider of thermal processing services in North America by a significant margin, with a comprehensive network coverage. This network offers more than 55 facilities convenient to customers in all areas where manufacturing and technical industries are concentrated.



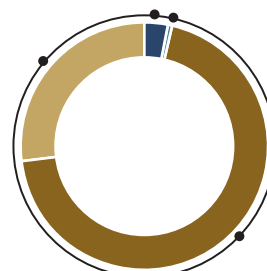
#### Revenue by market sector – £m North America

Aerospace and Defence	93.0
Energy	31.0
Automotive	65.5
General Industrial	66.1
<b>Total</b>	<b>255.6</b>

### Emerging Markets



Bodycote has more than 25 facilities in Emerging Markets covering Eastern Europe, China and Mexico. Bodycote is the number one thermal processing provider in Eastern Europe and is the leading Western provider in China.



#### Revenue by market sector – £m Emerging Markets

Aerospace and Defence	2.0
Energy	0.3
Automotive	44.0
General Industrial	17.0
<b>Total</b>	<b>63.3</b>

# Strategy and objectives

Bodycote's objective is to create superior shareholder returns through the provision of selected thermal processing services that are highly valued by our customers, giving full regard to a safe working environment for our employees and with the minimal environmental impact.

## Strategic priorities



### Driving operational improvement



### Capitalising on and investing in our Specialist Technologies



### Investing in Emerging Markets



### Investing in structural growth opportunities



### Acquisitions



### Safety & Environment



## Objectives

Continuous improvement of business processes and systems which make us more efficient and responsive.

Delivering unique solutions that provide customers with innovative, high value added products to meet the changing needs within component manufacturing.

Expanding with our customers in rapid growth countries with an emphasis on Eastern Europe, Mexico and China.

We invest in markets with long term structural opportunities such as the civil aviation market.

Adding bolt-on acquisitions to improve our plant network in Classical Heat Treatment, and investing in larger acquisitions and adjacent technologies to grow Specialist Technologies.

At the foundation of our business is the provision of a safe working environment for our employees, and to operate with minimal environmental impact.

Throughout this report you will see illustrations which link our business and strategy:

#### Strategy & Core Values



Aerospace, Defence & Energy



Automotive & General Industrial



Rapid growth countries



Technology



Customer service



Core values

#### Key Performance Indicators



Return on capital employed



Headline earnings per share



Return on sales



Free cash flow



Accident frequency



Carbon footprint

Read more information on our **Key Performance Indicators** on pages 12 and 13

# Our business model

Our business model is built around our priorities: being the supplier of choice and delivering operational excellence to our customers.

By continuing to meet our customers' needs and investing in our global network, we are well placed to create value in the long term.

## Provider of essential services to engineering manufacturers



### Classical Heat Treatment

- Working to very exacting quality specifications, heat treatment uses precisely controlled furnaces to process a huge variety of metals and alloys, improving their material properties.
- Bodycote's Classical Heat Treatments describe a group of mature heat treatment processes and include metal joining technologies which are used to join and assemble parts.

- Virtually every type of metal component, whatever its application, has received some form of processing before its introduction to service to enable it to perform to the required standard and last longer.

### Specialist Technologies

- Bodycote's Specialist Technologies refer to a group of processes which require very specialist expertise and technology. These technologies, some of which are proprietary, offer unique solutions for a variety of applications.



## The global leader

### Customer focus

- Bodycote is focused on continual improvement of our quality of service and takes an active role in finding solutions to technical issues and promoting mutual business development with our customers.
- Bodycote seeks to secure service-specific arrangements with our customers which provide protection from supply disruption by leveraging Bodycote's unique facility network.

### Global network

- Bodycote's global network of more than 180 market-focused facilities (see pages 6 and 7) in 23 countries brings economies of scale, particularly for logistics and equipment utilisation. This makes Bodycote's processing inherently more efficient than customers' in-house operations (see page 36) and competitors, thereby enhancing our competitive position in the subcontract market.
- The capital intensive nature of Bodycote's business also provides significant barriers to entry. The scope of Bodycote's network enables us to specialise more effectively than competitors at individual locations and provides comprehensive backup for our customers.

### Transferable know-how

- The global Bodycote network provides unique opportunities for the transfer of knowledge and skills, and the transfer of technology.
- With some of the best metallurgists, engineers and technicians in the industry, Bodycote is ideally placed to provide solutions for customers, wherever their market or wherever in the world they may be.
- Bodycote's scale enables continuous yet focused investment, both in the latest processes and in the most efficient and environmentally friendly equipment.



## The supplier of choice



### Service

- Bodycote has become the supplier of choice for many of the world's most respected and innovative engineering companies by providing highly efficient, cost-effective services to the highest quality standards through strategic investment in people and the latest technology, equipment and quality systems.

### Quality

- Bodycote's quality management systems, validated by major engineering OEMs, have been developed to meet the requirements of international and national accrediting bodies. All Bodycote facilities hold industry and customer approvals appropriate to the services they offer and the markets they serve.

### Expertise

- Bodycote's extensive facilities and expertise mean that projects can extend beyond customers' in-house capabilities, combining identification and provision of technical solutions which address in-service specification and deliver value-adding material properties.
- Our own enhancements and improvement of standard processes have led to Bodycote offering a range of proprietary processes which far outperform their standard counterparts.



## Creating value

### For customers

- Value-adding services
- Global supplier which can meet multiple processing needs
- Access to entire Bodycote knowledge base and expertise
- Cost and environmental benefits versus in-house operations

### For Bodycote

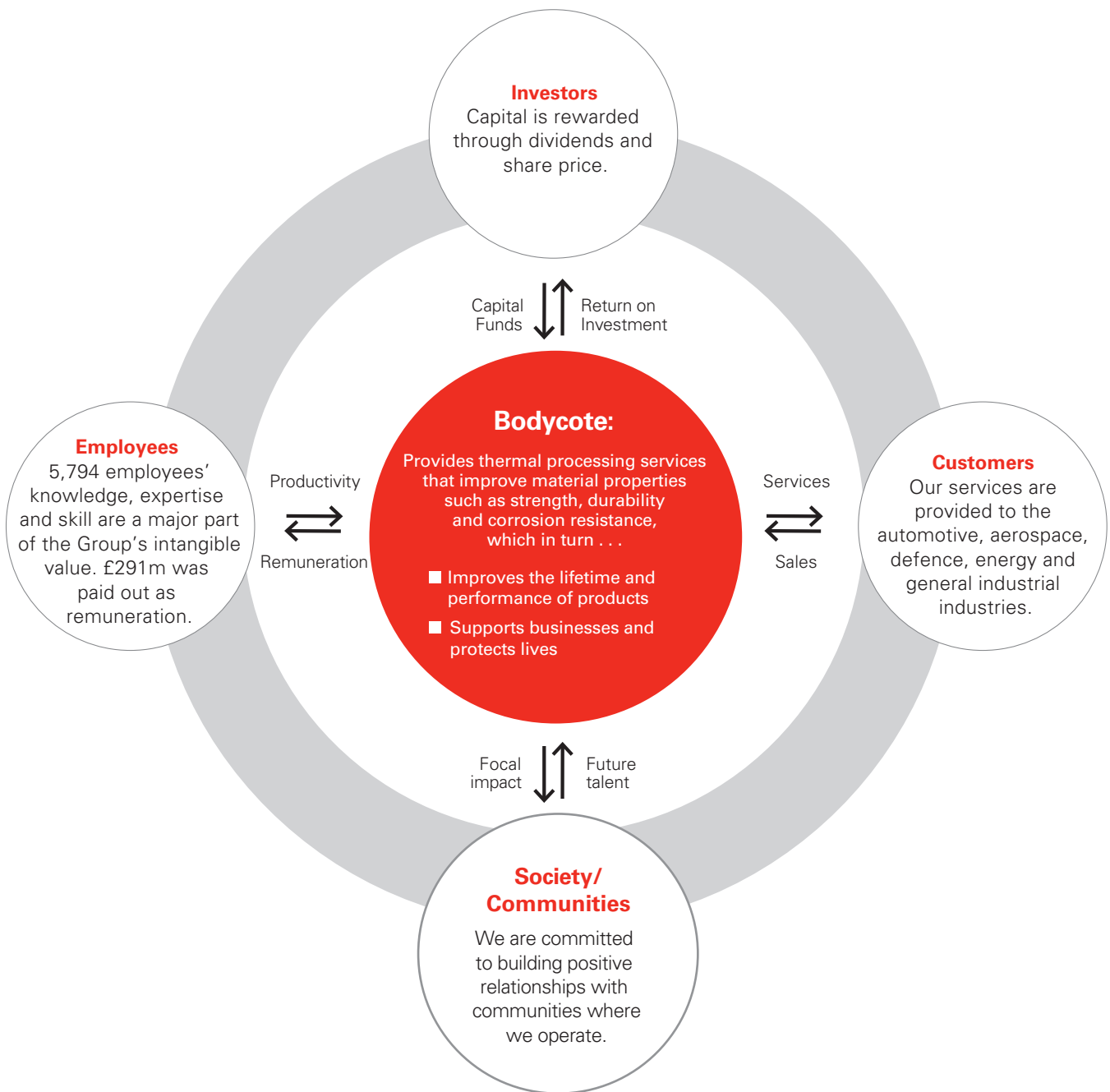
- Mutually beneficial customer relationships
- Wide customer base means Bodycote is not reliant on any one customer
- Ideally positioned to promote growth in emerging markets and selected technologies
- Clearly focused strategy

### For investors

- Financially stable and sustainable business
- Good growth drivers
- Superior return on investment
- Strong margins and cash flow

# Our stakeholders

Bodycote's stakeholder model shows how its interactions on various levels contribute towards socioeconomic growth and development. These exchanges, based on mutually beneficial relationships, provide the basis for the Group's growth and sustainability, which in return provides benefits to employees, investors, customers and society/communities.



## Investors

### Engagement undertaken

- Annual report and accounts/AGM
- Corporate website, including Investor Relations section
- Results presentation and post-results engagement with top shareholders
- Press releases (incl. LSE announcements)
- Addressing regular analysts' enquiries
- Capital markets day

### Reason for engagement

Continued access to capital is important to the long-term performance of our business. We work to ensure that our investors and analysts have a good understanding of our strategy and performance.

### Stakeholders' key interests

- Financial performance and economic impact
- Governance and transparency
- Sustainability of performance

## Customers

### Engagement undertaken

- Management of ongoing customer relationship
- Participation in industry forums/events
- Bodycote plc website 'www.bodycote.com' including the Annual and Interim Reports

### Reason for engagement

Engaging with our customers helps us to understand their needs and identify opportunities and challenges. We collaborate with our customers to improve our customers' product characteristics and to develop a project pipeline.

### Stakeholders' key interests

- Customer satisfaction
- Service performance, efficiency and quality
- Sustainable performance

## Employees

### Engagement undertaken

- Annual individual performance reviews
- Employee advisory councils
- Internal intranet and communications
- Annual report and accounts
- SHE briefings and toolbox talks
- Twitter and LinkedIn communications/Blogs

### Reason for engagement

Employee engagement is vital for our success. We work to create a diverse and inclusive workplace where every employee can reach their full potential. We engage with our people to ensure we are delivering to their expectations and making the right business decisions. This ensures we can retain and develop the best talent.

### Stakeholders' key interests

- Reputation
- Employee development/engagement
- Talent retention/Career opportunities
- SHE performance
- Diversity and inclusion

## Society/Communities

### Engagement undertaken

- Individual employee volunteering
- Corporate website

### Reason for engagement

We are committed to building positive relationships with the communities we operate.

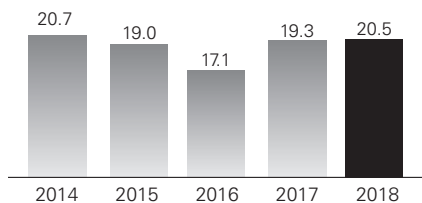
### Stakeholders' key interests

- Future talent pipeline
- Local operational impact
- Safety, health and environment performance

# Measuring progress

## Return on capital employed

(%)



## Performance

Return on capital employed increased by 1.2 percentage points during the year, from 19.3% to 20.5%.

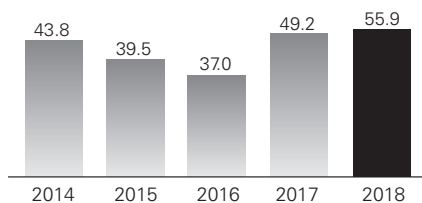
### Definition

Headline operating profit as a percentage of the average of opening and closing capital employed as adjusted for certain items of goodwill written off.

Capital employed is defined as net assets adjusted for net cash/(debt).

## Headline earnings per share

(pence)



## Performance

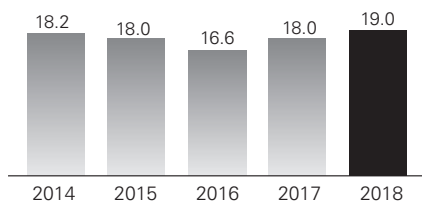
Headline earnings per share increased by 6.7p (13.6%) up from 49.2p to 55.9p.

### Definition

Headline earnings per share is defined in note 8 to the financial statements.

## Return on sales

(%)



## Performance

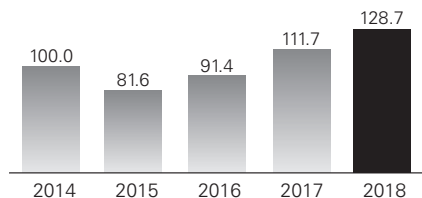
Return on sales increased by 1 percentage point during the year, from 18.0% to 19.0%. Headline operating profit increased by 12% from £123.9m to £138.3m, while revenue increased by 5.6% from £690.2m to £728.6m.

### Definition

Headline operating profit as a percentage revenue.

## Headline operating cash flow

(£m)



## Performance

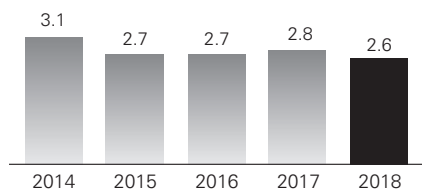
Headline operating cash flow for the Group was £128.7m (2017: £111.7m). This was 93% of headline operating profit (2017: 90%).

### Definition

Headline operating cash flow stated before cash flow relating to restructuring of £4.4m (2017: £3.7m) and acquisition costs of £0.5m (2017: nil).

## Total reportable case rate (TRC)<sup>1</sup>

(number)



## Performance

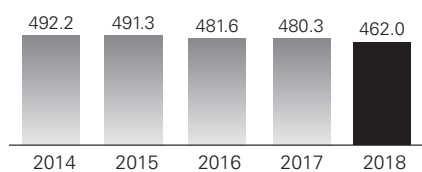
Bodycote works tirelessly to improve safety and reduce workplace incidents and is committed to providing a safe environment for everyone who works at or visits our locations. The TRC rate decreased to 2.6 this year (2017: 2.8). Further details are included in the corporate responsibility and sustainability section on page 34.

### Definition

TRC is defined as the number of lost time incidents, restricted work cases and medical treatment cases x200,000 hours (approximately 100 man years), divided by the total number of employee hours worked.

## Carbon footprint

(tonne CO<sub>2</sub>e/£m sales)



## Performance

On a normalised basis, the carbon footprint decreased by 3.8% from 480.3 tonnes per £m sales to 462.0 tonnes per £m sales. Further details are included in the Corporate responsibility section on page 34.

### Definition

Carbon footprint is defined as tonnes of CO<sub>2</sub> equivalent emissions divided by £m revenue. CO<sub>2</sub> equivalent emissions are calculated by taking electricity and gas usage in kilowatt hours and multiplying by country specific conversion factors provided by the International Energy Agency (IEA). Normalised emissions statistics restate prior year figures using current year country specific conversion (IEA) factors and current year average exchange rates.

# Specialist Technologies: Hot Isostatic Pressing (HIP Services)

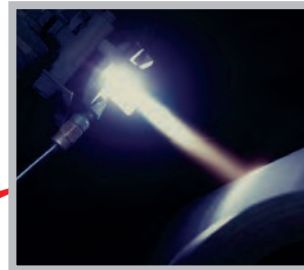
Hot Isostatic Pressing (HIP) combines very high temperature and pressure to eliminate porosity in castings and consolidate encapsulated powders to give fully dense materials. Dissimilar materials can be bonded together to manufacture unique, value-added components. With the largest operational capacity in the Western world, and a wide variety of sizes of equipment, Bodycote is able to accommodate large volumes of small product as economically as large individual components.

## INNER STRENGTH

The stress on a hip or knee joint when a person jumps off a chair is equal to around 100 tonnes per square inch. Our bones, effectively composites, absorb such stresses regularly and effectively for much of our lifetime. When joints fail, they are often replaced with metal alloy implants. These implants must be incredibly strong, biocompatible, and able to last the lifetime of the patient. A combination of heat treatment, hot isostatic pressing and coating makes this possible.



Cobalt chromium alloy billets are investment cast to form implant shape.



The castings are thermally sprayed with a biomedical coating to allow a bond to form between the implant and body tissue, promoting bone growth.



The implants are then HIPed to eliminate porosity, improve fatigue life and enhance the bonding of the biocompatible coating.



Solution and ageing heat treatment is used to strengthen the implant.



End application – joint replacement.



# Specialist Technologies: HIP PF inc. Powdermet®

HIP PF is additive manufacturing creating complex high integrity components from powdered metal in conjunction with HIP (Hot Isostatic Pressing) technology. HIP PF uses a variety of materials in powder or solid form and can be used to make components with the complexity of a casting but with the strength of a forging. It can be used to produce materials that can't be manufactured by any other means. Powdermet® technologies combine 3D printing with well-established net shape and near net shape techniques.

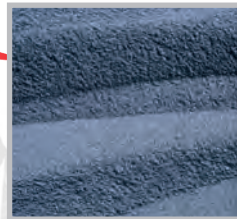
## Powder Power

### VALVE BODY

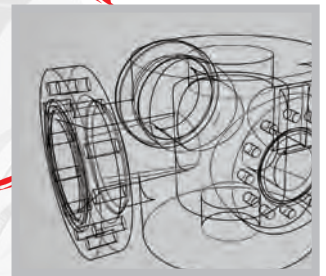
Valve components operating in the harsh environments of the oil & gas and chemical industries must withstand extreme material demands and resist attack from a variety of aggressive environments.

Bodycote Powdermet® technologies are a group of processes used in the production of complex components. These processes utilise near net shape (NNS), selective surface net shape (SSNS) and 3D printing techniques either in combination or on their own to produce cost-effective components with minimal production time. Powdermet® technologies\* produce fully consolidated components that cannot be manufactured to the same degree of complexity or material integrity by forging or casting processes.

\*Patents pending



The valve body begins life as high quality gas atomised stainless steel and nickel-based powders.



Following material selection, Bodycote's design engineers will work closely with customers to explore the unique and flexible component design opportunities afforded by Bodycote Powdermet® technologies. When the final NNS component design is received from the customer, Bodycote will create an engineering drawing.

The encapsulated valve is then HIPed using high temperatures and pressures which allows the powder to become 100% dense and form an NNS component.



The fabricated capsule, almost identical in shape to the finished component but larger in size, is filled with powder.



Finally the component can be pickled or machined to remove the capsule material resulting in a HIP NNS valve body which is inspected using ultrasonic testing techniques.



**End application – offshore oil, chemical or energy industries.**

# Specialist Technologies: Specialty Stainless Steel Processes (S<sup>3</sup>P)

S<sup>3</sup>P is a proprietary Bodycote treatment which offers unique surface hardening solutions for stainless steel, nickel-based alloys and cobalt-chromium alloys producing increased mechanical and wear properties without adversely affecting corrosion resistance. In all S<sup>3</sup>P processes, the corrosion resistance of the base material is not altered, while exhibiting superior wear resistance, strength and ductility, as well as resistance to galling.

## Bottle It

### DOSING DEVICE

There are several important factors influencing the productivity of machines used in the food and beverage industry. Of the utmost importance is cleanliness, not only from microbes but also from external pollutants from machine degradation.

For machines which operate 24/7 with production rates of several thousands of bottles per minute, equipment must perform faultlessly and be able to withstand aggressive wear and cleaning chemicals – Bodycote’s Specialty Stainless Steel Processes (S<sup>3</sup>P) provide the ultimate protection.



The device begins its journey as steel billet. Quality and purity of the steel is critical – it must be free from inclusions to generate a defect-free surface.



The device is machined to tight tolerances for shape and surface perfection to ensure no leaks in the equipment.



The device is vacuum annealed to eliminate machining stresses and to impart corrosion resistant properties.



The part is polished to a mirror finish to eliminate any remaining surface defects.



Bodycote’s S<sup>3</sup>P processing is applied to ensure the material can withstand the harsh conditions of high speed production, wear from food and drink, and attack from cleaning chemicals.



**End application – food and beverage production.**

# Specialist Technologies: Surface Technology

Specialised coatings are used to prolong the working life of components and protect them from environmental factors such as corrosion and abrasion. The range of coatings available includes thermally sprayed ceramic and metallic coatings and chemically formed ceramics. These covers a wide variety of applications, primarily in the aerospace, defence and energy markets.

## Controlling the Flow

### GATE VALVE

Gate valves and seats are used in the oil & gas industry to control the flow of oil-containing fluid extracted from the reserve. Within the well, pressures may be in excess of 15,000psi (or 6.5 tonnes per square inch) combined with high temperature. Such an extreme environment requires high performing components and reliable surface coating treatment. Bodycote applies a tungsten carbide coating to the valve and seat to provide a metal-to-metal seal that is highly wear and corrosion resistant.

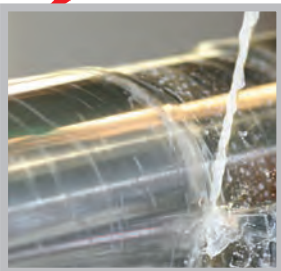


The valve component is machined from high grade stainless steel or nickel based alloy.

The coated surface is ground to specification to prepare it for polishing.



The valve component is coated with gas tight tungsten carbide to provide a wear and corrosion resistant surface.



The part is super polished to provide a metal-to-metal sealing surface capable of withstanding pressures in excess of 20,000psi.



The part is assembled into the operating control valve and leak checked.



End application – subsea assembly or land-based rig.

# Specialist Technologies: Low Pressure Carburising (LPC)

LPC is a case hardening process carried out in a vacuum furnace using hydrocarbon gases at very low pressure and elevated temperatures to obtain a hardened surface layer and a tough core. This 'clean' treatment is used to increase the wear resistance and fatigue life of components.

## In Gear

### PINION GEAR

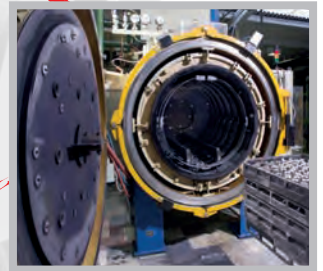
A pinion gear is a critical automotive component used in virtually all transmission units. During use, a vehicle places heavy demand on its transmission, requiring a fast and reliable response to the drive controls.

The gears require high strength and wear resistance in order to withstand the stresses applied to each gear during use. Bodycote's heat treatment processes, in particular Low Pressure Carburising (LPC), enable modern transmissions to deliver high performance and seamless response, even reducing noise during gear changes.

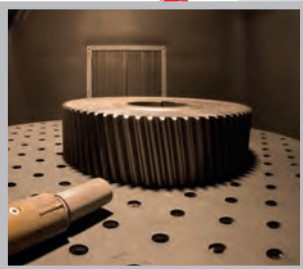


The gears begin life as low alloy steel.

The gears are quenched using Nitrogen gas to minimise part distortion, then tempered to relieve internal stresses.



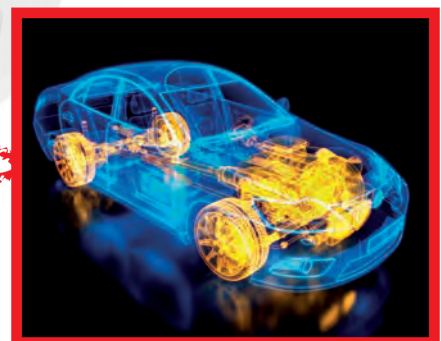
The gears are dimensionally measured before heat treatment to monitor and maintain repeatability of distortion. The gears are then heat treated using LPC to enhance functionality by adding a 'case depth' to provide strength and resistance to wear and tear.



The gears are shot peened to add residual stress – this allows the parts to withstand more wear and tear. The gears are measured again after heat treatment to check any distortion is within limits.



The gears are assembled into the transmission unit.



End application – automobile.

# Specialist Technologies: CiD®

CiD® is a proprietary Bodycote thermochemical heat treatment for simultaneous improvement of corrosion resistance and wear properties through generating an iron nitride-oxide compound layer on steel. CiD® is favoured for components that are subjected to a corrosive environment in combination with wear.

## Stress Ball

### BALL STUDS

Used in virtually every automobile made, ball studs are located within the ball joints in a vehicle's steering system, between the wheels and suspension, allowing rotating movement – similar to the way a human hip joint works. Because of their function and position within the vehicle, they must be extremely strong, corrosion resistant and able to cope with weight and stress. Their effective operation is critical to the safety of the vehicle and, therefore, the driver. Bodycote's proprietary CiD® process ensures the parts achieve the necessary material properties.

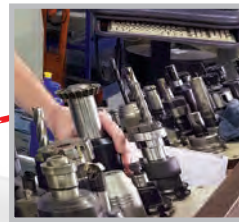
The ball studs are cold forged from heat treatable steel.



The parts are quenched and tempered to obtain the necessary core material strength.



The ball studs receive Bodycote's proprietary CiD® process to improve their corrosion resistance and hardness.



The part surface is machined and roller burnished.

The parts are polished to achieve specified roughness values – essential for the function of the joint and the steering behaviour of the vehicle.



The parts are inspected and tested for roughness, surface and core hardness, and corrosion resistance.



End application – vehicle.

# Chair's statement

"I continue to be impressed with the commitment, passion and knowledge of Bodycote employees at all levels from across the Group"

**A. C. Quinn CBE**  
Chair



## Overview

Bodycote delivered a good performance in 2018, with management continuing to implement the Group's Strategy. I am very pleased to note how well the management team continues to drive the business forward, delivering on our commitments and investing to support future growth opportunities for our business.

## Dividend

The Board is proposing a final dividend of 13.3p, an increase of 10%, which will be paid on 7 June 2019, subject to shareholder approval at the 2019 Annual General Meeting (AGM). This brings the total ordinary dividend for 2018 to 19.0p (2017: 17.4p) costing £36.1m which represents a year on year increase of 9.1%. This increase in the level of dividend underscores the Board's view of the Group's excellent future earnings and cash flow potential.

Furthermore, in keeping with our current policy of sweeping cash remaining at year end for which we see no immediate use the Board is recommending a supplemental distribution by way of a special dividend, also payable on 7 June 2019 of 20.0p per share, costing £38.3m.

## Board and governance

The Board is mindful of the 2018 corporate governance code and changes in legislation introduced during the year that are intended to encourage responsible corporate behaviour. Bearing this in mind, we have incorporated information on our stakeholders and stakeholder engagement in this Annual Report.

One of the key roles of Chair is to ensure that the Board members possess a range of complementary skills which are relevant to Bodycote's business. After completing my first year as Chair and spending considerable time with my Board colleagues I am confident that we have a well-balanced Board that, in terms of governance, is functioning effectively.

During the year, the Board also underwent an external board evaluation, which is conducted every three years. I am pleased to report that the results of the review were very positive. And as always, there were a number of observations and recommendations that we have carefully evaluated to ensure that the Board is as effective as possible in exercising its various responsibilities.

As Chair, I have a responsibility to promote effective governance across the Group to ensure we remain a successful and sustainable entity with good governance procedures across all 23 countries of operation. We are committed to conducting business responsibly. By maintaining these high standards of corporate governance we are able to enhance business performance underpinned by our business model. The approach to Governance is set by the Board and implemented by our Executive Committee. Effective and robust governance remains a strong pillar supporting the sustainable success of the Group.

## People

During the year, I have continued to visit many of our facilities around the world and engaged with many of our executives and management. I continue to be impressed with the commitment, passion and knowledge of Bodycote employees at all levels from across the Group and appreciate that our talented workforce is key to Bodycote maintaining its market position and the long term success of the business.

## Shareholders

Meetings with shareholders have taken place throughout the year with very positive feedback and I look forward to seeing more of you during the coming year and at this year's AGM in May 2019.

## Summary

Our strategy is designed to generate superior margins and returns through strong service delivery and operational efficiency. We aim to drive revenue growth through investments to support markets with structural growth (e.g. civil aviation), growth in our Specialist Technologies business, and targeted investment in rapid-growth Emerging Markets. The results in 2018 demonstrate continued progress in each of these areas.

The Company remains well positioned to deliver attractive returns for our shareholders.

**A.C. Quinn CBE**  
Chair  
8 March 2019

# Chief Executive's review

"We achieved double-digit growth in Specialist Technologies' revenues, an excellent performance in our Emerging Markets and robust growth in civil aviation revenues. Our performance is testament to the Group's resilient operating model, with our focus on cashflow generation, operational efficiency and improving returns."

**S. C. Harris**  
Group Chief Executive



## Overview

Bodycote reported revenue growth of 5.6% to £728.6m (2017: £690.2m). Constant currency revenues grew 6.7%. Headline operating profit increased 12% to £138.3m (£123.9m) and return on sales further improved to 19.0% (2017: 18.0%). Statutory operating profit also increased 12% to £134.1m.

The following reflects constant currency growth rates unless stated otherwise.

Our Specialist Technologies delivered double digit growth of 12%, reflecting continued adoption of these technologies supported by ongoing investment in new capacity and capability. We achieved strong growth of 21% in our rapid growth Emerging Markets. This was helped by solid contributions from recent greenfield start ups, in particular in Mexico and China. We continued to invest in the structural growth opportunity represented by the civil aviation market where our revenues grew 8%.

Our return on sales continues to expand, reflecting our multiyear programme of pricing and efficiency improvements in the AGI Classical Heat Treatment business aimed at improving the quality of this business to a similar level to the ADE business. The movement in revenue mix in favour of our higher margin Specialist Technologies also added to the improvement in return on sales and is part of our long term goal of improving Group margins to world class levels.

The cash generative nature of Bodycote's business was underlined by the 93% headline operating cash conversion, and ROCE further improved to 20.5% from 19.3% in 2017. We delivered £97m of free cash after investing £44m in capacity and capability expansion, which will enable us to continue our earnings growth in future years.

## Our Technologies

The Classical Heat Treatment (CHT) business contributed 76% of total Group revenues, with growth of 5%, reflecting growth across all our key market sectors.

We achieved 12% growth across our Specialist Technologies, which constitute 24% of the Group's revenues. Low Pressure Carburising (LPC) and Corri-i-Dur® (CiD®) both grew revenues over 20% and HIP Product Fabrication (HIP PF), grew over 30%. This reflects increased adoption of these differentiated technologies and is supported by investment in additional capacity across our network.

## Emerging Markets

A key pillar of our strategy is targeted investments in rapidly growing Emerging Markets. Our revenues in these markets grew 21%. This growth was underpinned by buoyant performances in Mexico, as automotive exports to the USA increased, and from China where we are achieving increased penetration of the automotive market. Emerging Markets now represent 9% of Group revenues, up from 7% in 2016 (and up from 2% in 2009). Continued investment in these markets should sustain good growth into the future.

# Chief Executive's review continued

## Market Sectors

Civil aviation revenues grew 8% in the year, with 12% growth in the second half as industry supply chain problems eased. The UK operations performed strongly again, supported by additional capacity in the final quarter of the year with our new aerospace facility in Rotherham (UK) coming on line. North American revenues also continued to build as production of LEAP engines ramped up and the supply chain bottle necks for titanium castings have started to ease.

General industrial markets represent 38% of Group revenues, serving a very broad range of industrial sectors. Revenues grew 6% in the year, representing further solid growth across our key geographies.

Revenues from the energy sector grew 13% in the year, notwithstanding the well publicised substantial fall in revenues from the large-frame industrial gas turbines' (IGT) original equipment manufacturers. Growth came predominantly from buoyant oil & gas revenues, much of it driven by demand in the Permian basin, although there was some evidence of customers de-stocking towards the end of the year. In the latter part of the year, revenues benefited from shipments on HIP PF subsea contracts that had been won earlier in the year. The order book in subsea work continues to grow at an increasing rate.

The automotive business grew 7%. This was another strong performance against the backdrop of flat markets in both Western Europe and North America, reflecting the excellent growth of Specialist Technologies in the sector.

## Investment in growth

During the year, we invested £44m (more than 50% of overall gross capex) across our entire business to support future growth, adding new capacity into existing facilities, as well as developing new facilities. It takes some time to build a new facility and subsequently typically takes a further three to five years for revenues to fully mature. Since the beginning of 2016, we have opened nine new facilities, focused on market sectors with long term structural growth, expanded our footprint in rapid growth Emerging Markets, and grown our Specialist Technologies' businesses. These facilities, which are strongly underpinned by contracts from anchor customers, are contributing meaningfully to the Group's revenue growth as they ramp up.

We acquired a Classical Heat Treatment facility in the United States of America towards the end of the year, which will fit well with our existing business in the South East, enhancing growth and operating efficiency.

We also have an exciting pipeline of new investments, including new facilities being built in Illinois and New York (USA), in Italy and new facilities in the Emerging Markets of Hungary and Czech Republic. Furthermore, we are adding additional HIP capacity into the USA and European markets to meet civil aviation demand.

## Profit and Earnings

As expected, we experienced higher input cost inflation in a number of our markets, with pressure coming from tighter labour markets, and cost increases in utilities and industrial gases that we use in our processes. We continue to proactively manage this to ensure that the value of our price increases at least offsets the cost increases incurred.

The Group's profit improvement, coupled with a headline tax rate of 21.7% (2017: 22.9%), increased basic headline earnings per share to 55.9p (2017: 49.2p). Basic earnings per share increased to 54.2p (2017: 51.0p).

## Strategic Progress

The Group's strategy encompasses the drive for operational efficiency and delivering strong return on sales and good return on capital employed. The Group is committed to invest to support profitable growth. The priorities for growth are capacity and capability enhancement in Specialist Technologies, expansion of the Group's footprint in rapid growth Emerging Markets and investment in markets with long term structural growth such as civil aviation and growth through targeted acquisitions. The Group has a minimum 20% hurdle rate return when appraising investments.

During 2018, we made continued progress against our strategy, delivering both higher return on sales of 19.0% (2018: 18.0%) and an increase in ROCE to 20.5% (2018: 19.3%).

Civil aviation revenue grew 8%, Emerging Markets revenues grew 21%, and Specialist Technologies grew 12%, which all reflect the success of the investment focus of the Group in these businesses over a number of years.

We continue to look at acquisition and investment opportunities. These are traditionally bolt-on facilities that can provide us with infills to our existing network. Where the opportunities to buy such facilities with good prospects do not exist we will build new facilities. Newly constructed facilities have a ramp up period, but have the advantage of being designed exactly in line with the Group's technology and operational efficiency focus. Since 2014, we have invested over £210m in both acquisitions and investment for growth in new and existing facilities. The growth noted above in civil aviation revenues, Emerging Markets revenues and Specialist Technologies revenues, have all been boosted by these investments. In many cases, the revenues from these past investments are still ramping up and so will contribute to growth in revenue and profit in the coming years.



## Organisation and people

Bodycote is a service business and our first-class service is delivered by committed individuals, who understand their customers' needs and meet their demanding and changing requirements on a continual basis. Our people are the cornerstone of the business and it is through their endeavours, day in and day out, that we create value and deliver our objectives. Developing our employees to ensure that our talented workforce remains one of our competitive advantages is a priority for the Group.

## Summary and Outlook

2018 has once again demonstrated the strength of Bodycote's strategy and business. We achieved double-digit growth in Specialist Technologies revenues, an excellent performance in our Emerging Markets and robust growth in civil aviation revenues.

Combined with pricing discipline in the face of significant cost pressures, the Group was able to improve return on sales. Together with the revenue growth this delivered a healthy increase in headline earnings per share. Our performance is testament to the Group's resilient operating model, with our focus on cashflow generation, operational efficiency and improving returns.

While we are conscious of the global macro-economic backdrop, we have entered 2019 well positioned and at this early point in the year, our expectations for 2019 remain unchanged.

### S.C. Harris

Group Chief Executive  
8 March 2019

# Business review

## The ADE Business



Bodycote has more than 40,000 customers serviced by more than 180 facilities around the world. These facilities are organised into two customer focused businesses; the ADE business and the AGI business. Our ADE business is focused on aerospace, defence and energy customers, who tend to think and operate globally.

Strategically we have focused on building customer relationships to enable our participation in long term programmes particular in the civil aviation market. Not only do we have a competitive advantage as a result of our scale and capabilities, but our global reach allows customers to work with us on multiple projects simultaneously, making us a valued business partner.

A large number of Bodycote's global customers fall within our ADE business and Bodycote intends to continue to leverage its unique market position to increase revenues in the aerospace, defence and energy sectors. We have more than 60 facilities around the world including Hot Isostatic Pressing (HIP) and Surface Technology facilities, alongside our Classical Heat Treatment plants.

The following review reflects constant currency growth rates unless stated otherwise.

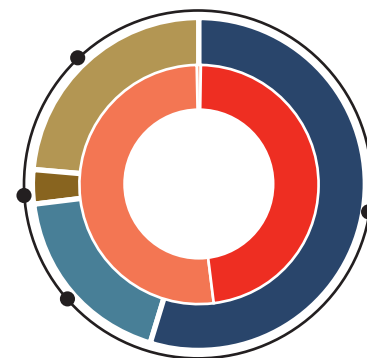
Revenue in 2018 was £288.0m, an increase of 7% (5% at actual rates). Civil aviation registered good growth, particularly in the second half of the year as some of the supply chain issues that have been holding back industry growth appeared to ease, particularly in North America. Oil & gas revenues also registered strong growth, while revenues from Industrial Gas Turbines declined as the OEMs cut back on production.

Headline operating profit was £68.7m, an increase of 8% (7% at actual rates). Consequently, return on sales improved to 23.9% (2017: 23.5%). Statutory operating profit grew to £67.8m (2017: £62.7m).

Net capital expenditure in 2018 was £25.3m (2017: £32.1m), representing 1.1 times depreciation. We have invested in new HIP capacity in North America and Europe, as well as opening a new facility in Rotherham, UK to support the growth in the civil aviation business.

Return on capital employed increased to 21.7% (2017: 21.4%), with improved profitability and continued careful management of the balance sheet.

### ADE revenue by market sector and geography £m



#### Market sector

■ Aerospace and Defence	158.0
■ Energy	52.8
■ Automotive	9.9
■ General Industrial	67.3
<b>Total</b>	<b>288.0</b>

#### Geography

■ Western Europe	137.7
■ North America	149.1
■ Emerging Markets	1.2
<b>Total</b>	<b>288.0</b>

# Business review

## The AGI Business



Bodycote has more than 40,000 customers serviced by more than 180 facilities around the world. These facilities are organised into two customer focused businesses; the ADE business and the AGI business. Our AGI business is focused on automotive and general industrial customers. These include many multinational businesses which tend to operate on a regionally-focused basis, as well as numerous medium sized and smaller businesses, all of which are important to Bodycote. Much of the AGI business is locally oriented.

Strategically we have focused on building customer relationships to enable our participation in long term programmes. Not only do we have a competitive advantage as a result of our scale and capabilities, but our global reach allows customers to work with us on multiple projects simultaneously, making us a valued business partner.

Our extensive network of more than 120 AGI facilities enables the business to offer the widest range of capability and security of supply. Bodycote has a long and successful history of servicing its wide-ranging customer base.

The following review reflects constant currency growth rates unless stated otherwise.

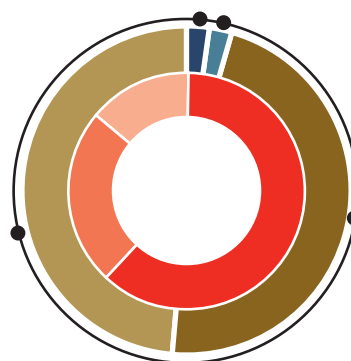
Revenue was £440.6m, 7% ahead of the prior year (6% at actual rates). Western Europe delivered solid growth, driven by a strong performance in the first half of the year. North America also registered robust growth through the year. Once again, Emerging Markets were the standout performer, registering growth above 20% and now representing 14% of total divisional revenues, driven by strong performances in Mexico and China.

Headline operating profit was £82.4m (2017: £74.2m), 12% ahead of the prior period (11% at actual rates). Return on sales expansion has been a focus for our AGI business over many years and we continued this trend, reporting further improvement to 18.8% (2017: 17.8%). Statutory operating profit grew to £79.6m (2017: £71.2m).

Net capital expenditure was £50.2m (2017: £37.8m) representing 1.3 times depreciation. We are continuing to invest in the rapid growth Emerging Markets, our Specialist Technologies and investing in new facilities alongside investment in new capacity in existing facilities.

Return on capital employed increased to 20.1% (2017: 17.8%), further augmenting last year's improvement and hitting the Group's hurdle return on capital employed for the first time since the AGI business structure was created.

### AGI revenue by market sector and geography £m



#### Market sector

■ Aerospace and Defence	10.5
■ Energy	9.8
■ Automotive	206.3
■ General Industrial	214.0
<b>Total</b>	<b>440.6</b>

#### Geography

■ Western Europe	272.0
■ North America	106.5
■ Emerging Markets	62.1
<b>Total</b>	<b>440.6</b>

# Chief Financial Officer's report



**Dominique Yates**  
Chief Financial Officer

## Financial overview

	2018 £m	2017 £m
Revenue	<b>728.6</b>	690.2
Headline operating profit	<b>138.3</b>	123.9
Amortisation of acquired intangible fixed assets	<b>(3.7)</b>	(4.5)
Acquisition costs	<b>(0.5)</b>	-
Operating profit	<b>134.1</b>	119.4
Net finance charge	<b>(1.9)</b>	(2.4)
Profit before taxation	<b>132.2</b>	117.0
Taxation	<b>(28.6)</b>	(19.7)
Profit for the year	<b>103.6</b>	97.3

Group revenue was £728.6m, an increase of 5.6% at actual exchange rates, and 6.7% at constant currency. New facilities contributed 1.6% to revenue growth.

Headline operating profit for the year increased by 12% to £138.3m (2017: £123.9m), and return on sales increased to 19.0% (2017: 18.0%). Price increases once again more than covered the increase in input costs. Statutory operating profit grew 12% to £134.1m (2017: £119.4m).

## Finance charge

The net finance charge was £1.9m compared to £2.4m in 2017, analysed as follows:

	2018 £m	2017 £m
Interest received on bank overdrafts and loans	0.2	0.1
Net interest payable <sup>1</sup>	0.1	0.1
Financing and bank charges	1.8	2.0
Pension finance charge	0.2	0.4
<b>Total finance charge</b>	<b>2.1</b>	<b>2.5</b>
<b>Net finance charge</b>	<b>1.9</b>	<b>2.4</b>

1. Amounts arising on financial liabilities measured at amortised cost.

As at 31 December 2018, the Group's £230m Revolving Credit Facility is totally undrawn and has a remaining life of 3.3 years.

## Profit before Taxation

	2018 £m	2017 £m
Headline profit before taxation	136.4	121.5
Amortisation of intangibles	(3.7)	(4.5)
Acquisition costs	(0.5)	-
<b>Profit before taxation</b>	<b>132.2</b>	<b>117.0</b>

Statutory profit before tax increased to £132.2m (2017: £117.0m), while headline profit before tax increased 12% to £136.4m (2017: £121.5m).

## Tax

The headline tax rate for the Group fell to 21.7% (2017:22.9%) as a result of the reduction in the US Federal corporate income tax rate.

However, the statutory tax rate of 21.6% increased from that of 16.8% in 2017, since the 2017 tax charge benefited from a one-off tax gain of £6.4m as a result of a revaluation of the Group's deferred tax liabilities, following the passing of the Tax Cuts and Jobs Act in the US in December 2017.

Some clarifications on implementation of the US Tax Cuts and Jobs Act were issued in December 2018. While these only apply from 2019, the impact will likely be a reduction in benefit to Bodycote from the financing activities into the US, as the ability to take tax deductions for interest is restricted. This is a trend common across tax legislation developments everywhere, including other jurisdictions where Bodycote operates.

The Group's statutory tax rate is impacted by a certain level of taxation risk related to the jurisdictions in which the Group operates. Provisions of £16.1m are carried in respect of potential future additional tax assessments related to 'open' historic tax years. Reference is made to note 6 of the financial statements for more information.

## Earnings per Share

The improved Group business performance drove basic headline earnings per share up to 55.9p (2017: 49.2p) while basic earnings per share for the year increased to 54.2p (2017: 51.0p).

	2018 £m	2017 £m
Profit before taxation	132.2	117.0
Taxation	(28.6)	(19.7)
<b>Profit for the year</b>	<b>103.6</b>	<b>97.3</b>
Basic headline EPS	55.9p	49.2p
<b>Basic EPS</b>	<b>54.2p</b>	<b>51.0p</b>

## Return on Capital Employed (ROCE)

The return on capital employed rose in the current year to 20.5% from 19.3% in 2017. This improvement was driven by the increase in the Group's operating profit. Moreover, since 2014, the Group has invested over £215m on acquisitions and expansionary investment projects, many of which are not yet fully mature and are not contributing as fully to Group returns as they will once they have all reached financial maturity. The Group continues to exert strong financial discipline in the area of capital expenditure, applying stringent financial returns hurdles to all of its projects.

## Cash Flow

	2018 £m	2017 £m
Headline operating profit	138.3	123.9
Add back non-cash items:		
Depreciation and amortisation	62.0	59.8
Impairment of fixed assets	1.8	0.4
Share-based payments	3.8	7.8
Profit on disposal of property, plant and equipment	(1.7)	(0.7)
Loss on disposal of businesses	0.6	-
<b>Headline EBITDA<sup>1</sup></b>	<b>204.8</b>	<b>191.2</b>
Net capital expenditure	(74.0)	(74.8)
Net working capital movement	(2.1)	(4.7)
<b>Headline operating cash flow</b>	<b>128.7</b>	<b>111.7</b>
Cash cost of restructuring	(4.4)	(3.7)
Acquisition costs	(0.5)	-
<b>Operating cash flow</b>	<b>123.8</b>	<b>108.0</b>
Interest paid	(1.9)	(2.1)
Taxation	(24.5)	(22.9)
<b>Free cash flow</b>	<b>97.4</b>	<b>83.0</b>
Acquisition spend	(8.3)	(14.2)
Disposals	0.7	-
Ordinary dividend	(34.2)	(30.6)
Special dividend	(47.6)	-
Own shares purchased	(10.6)	-
Other	(0.1)	0.3
<b>(Decrease)/increase in net cash</b>	<b>(2.7)</b>	<b>38.5</b>
Opening net cash	39.6	1.1
Loans acquired with subsidiaries	(0.7)	-
<b>(Decrease)/increase in net cash</b>	<b>(2.7)</b>	<b>38.5</b>
<b>Closing net cash</b>	<b>36.2</b>	<b>39.6</b>

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

The Group's headline operating cash flow increased 15% to £128.7m, mainly reflecting the improvement in the headline operating profit. Headline operating cash conversion was 93% as the Group continued to demonstrate an impressive record of converting profit into cash. Consequently, free cash flow increased 17% to £97.4m. Net cash from operating activities increased 8% from £159.9 to £173.3m. The Group ended 2018 with £36.2m of net cash, only slightly lower than 2017 (£39.6m) despite paying ordinary and special dividends totalling £81.8m, and investing £44.1m in expansionary capital expenditure projects during the year.

# Chief Financial Officer's report continued

## Capital expenditure

Net capital expenditure (capital expenditure less proceeds from asset disposals) for the year was £74.0m (2017: £74.8m). The multiple of net capital expenditure to depreciation was 1.2 times (2017: 1.3 times).

As noted above, £44.1m of capital expenditure was invested in expansionary projects, in line with our strategy to invest for profitable growth, particularly in new facilities and incremental capacity for Specialist Technologies, in several new facilities in Emerging Markets and to support the long-term structural growth opportunity in the civil aviation market. Alongside this, the Group continues to invest in maintaining its assets to a high quality, with repairs and maintenance costs also being expended directly in the Group's profit and loss account.

## Acquisitions and Disposals

We acquired a small facility in the US towards the end of the year, which fits well with our existing business in the South East, enhancing growth opportunities and helping with operating efficiency. In addition, we disposed of two small non-core businesses in France and Germany. Net consideration totalled £8m.

## New standards

A new IFRS standard on the accounting of leases (IFRS 16) will impact Bodycote's accounts in 2019. While it does not change the underlying nature of our business at all, from an accounting perspective, it recognises leased assets as 'right of use' assets held on the balance sheet and classifies future lease liabilities as a financial liability. This will have the impact of adding c£80m to the Group's financial liabilities (based on leases we held at the end of 2018). In the P&L, it will add c£2m to Headline Operating Profit, with a similar increase in finance charges, leaving Profit before Tax and Earnings per Share measures unchanged.

During 2018, IFRS 9 (Financial instruments) and IFRS 15 (Revenue from contracts with customers) were adopted, with an immaterial impact on the Group's accounts.

## Dividend and Dividend Policy

The Group aims to pay ordinary dividends so that dividend cover will be at or above 2.0 times earnings. The Board may also recommend payment of a supplemental distribution to shareholders. The amount of any supplemental distribution will be assessed in light of the cash position of the Group, along with funding requirements for both organic growth and acquisitions.

In line with this policy, the Board has recommended a final ordinary dividend of 13.3p (2017: 12.1p), bringing the total ordinary dividend to 19.0p (2017: 17.4p). In addition, in light of the Group's strong balance sheet and year end net cash position, the Board has recommended a special dividend of 20.0p (2017: 25.0p). If approved by shareholders, both the final ordinary dividend and the special dividend will be paid on 7 June 2019 to shareholders on the register at the close of business on 23 April 2019.

## Borrowing Facilities

The Group is financed by a mix of cash flows from operations, short-term borrowings, long-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. The Group continues to have access to committed facilities at competitive rates and therefore currently deems this to be the most effective means of long-term funding.

The total undrawn committed facility funding available to the Group at 31 December 2018 was £230.0m (2017: £230.0m). At 31 December 2018, the facility was undrawn.

Facility	Expiry date	Facility £m	Facility utilisation £m	Facility headroom £m
£230m Revolving Credit	3 April 2022	230.0	-	230.0

## Post balance sheet events

There are no post balance sheet events that require disclosure in the financial statements.

## Alternative performance measures

Bodycote uses alternative performance measures such as headline operating profit, headline earnings per share, headline profit before taxation, headline operating cash flow and free cash flow, together with current measures restated at constant currency. These assist users of the financial statements to gain a clearer understanding of the underlying performance of the business, allowing the impact of restructuring and reorganisation activities and acquisition costs to be identified separately. These alternative performance measures can be found in Note 1 to the accounts.

## Going concern

In determining the basis of preparation for the Annual Report and the Group's viability statement, the directors have considered the Group's business activities, together with the factors likely to affect its future development, performance and position. This includes an overview of the Group's financial position, cash flows, liquidity position and borrowing facilities.

The Group meets its working capital requirements through a combination of cash resources, committed and uncommitted facilities, and overdrafts. The overdrafts and uncommitted facilities are repayable on demand but the committed facilities are due for renewal as set out below. There is sufficient headroom in the committed facility covenants to assume that these facilities can be operated as contracted for the foreseeable future.

The committed facilities as at 31 December 2018 were as follows:

- £230m Revolving Credit Facility maturing 3 April 2022

The December 2018 weighted average life of the committed facilities was 3.3 years.

The Group's forecasts and projections, taking account of reasonable potential changes in trading performance, show that the Group should be able to operate within the level of its current committed facilities.

The directors have reviewed forecasts and projections for the Group's markets and services, assessing the committed facility and financial covenant headroom, central liquidity and the Group's ability to access further funding. The directors also reviewed downside sensitivity analysis over the forecast period, thereby taking into account the uncertainties arising from the current economic environment. Following this review, the directors have formed a judgement, at the time of approving the 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 financial statements.

## D. Yates

Chief Financial Officer  
8 March 2019

# Principal risks and uncertainties

The Board is responsible for the Group's risk management and determining the Group's risk appetite. The review of financial risk has been delegated to the Audit Committee. The Group's risk framework, using a variety of top down and bottom up approaches, is used to identify, monitor and report risks. The risks are aggregated first at a divisional level and then at Group level. For each business critical risk, assurance activities have been documented in risk assurance maps and these are used to direct assurance activity including that of Internal Audit.

The Group Head of Risk is supported by the Risk and SHE Committee, which met three times during 2018, attended by a Vice President from each of the operating divisions, the Group Head of SHE and the General Counsel. The Risk and SHE Committee assists the Group Head of Risk in identifying critical risks, embedding risk management and facilitating the implementation of risk management measures throughout the Group. The Group Head of Risk provides an update to the Executive and Audit Committees on the Group's risk activities at every meeting and a comprehensive review of the Group's business critical risks is presented to the Board in June and in December. The Board concluded that an ongoing process of identifying, evaluating and managing the Group's significant risks has been in place throughout 2018 and a robust assessment of the principal risks had been undertaken.

The table below highlights the major risks that may affect Bodycote's ability to deliver the strategy, as laid out on page 8. These risks have been reviewed throughout the year and no risks have been added or removed since 2017. The two risks added in 2017, Environmental and Capital Projects, have been subject to risk deep dives by the Board during 2018.




In July 2018, a fire occurred at the Syracuse facility in New York State resulting in the total loss of the facility. Bodycote personnel responded safely and quickly to ensure the continuity of service for customers. The Group's business continuity framework responded and customers' parts are being treated at other Bodycote facilities.

Per the criteria that the Board has agreed to assess potential risks, they may be classified as principal risks by virtue of their potential financial impact on the Group in the foreseeable future, in combination with the likelihood of this impact occurring.




The Board has examined and assessed the potential risks facing the Group as a result of the 2016 referendum on the future of the UK's membership in the European Union. These risks included potential impacts on future performance and business model considerations. The Board does not expect this will have a material impact on Bodycote as customers are served locally and therefore cross-border trading is not material.

In determining the Group's principal risks, The Board also examined and assessed the potential risks to the Group posed by the wider effects of climate change on Bodycote's business. The Board concluded that the effects of climate change do not qualify as a principal risk for the Group.


Details of the Group's financial risks (funding, foreign exchange, interest rate and counterparty risks), which are managed by the Group's treasury function, are provided in note 18 to the financial statements. The mitigating activities described below will help to reduce the impact or likelihood of the major risk occurring, although the Board recognises that it will not be possible to eliminate these risks entirely. The Board recognises that there could be risks that may be unknown or that may be judged to be insignificant at present but may later prove to be significant. For this reason business continuity plans have been prepared for all plants to provide for situations where specific risks have the potential to severely impact the business.

Risk description	Impact	Mitigation and control	Relevance to strategy
<b>Market and customer risks</b>			
<p><b>Markets</b></p> <p>Bodycote operates in 23 countries and the Group's revenues can be expected if macroeconomic trends, as well as the life cycles of the different components at the Group. The result of the referendum on the future of the UK's membership of the European Union is not expected to have a material transactional impact as customers are typically served locally and cross-border trading is not material.</p>	<p><b>Stable</b></p> <p>The high proportion of short-term fixed costs in the business means that a drop in sales will have a significant impact on profitability.</p>	<ul style="list-style-type: none"> <li>■ Bodycote's presence in 23 countries servicing more than 40,000 customers across a wide variety of end-markets acts as a natural hedge to neutralise localised economic volatility and component life cycles.</li> <li>■ There is some short-term flexibility in the cost base (e.g. by ensuring that a proportion of the workforce is employed on temporary contracts) and changes in customer demand are responded to quickly.</li> <li>■ It should be noted that revenues for the UK represent only 8% of Group revenues, with the significant majority of its business coming from UK customers.</li> </ul>	  



# Principal risks and uncertainties continued


Risk description	Impact	Mitigation and control	Relevance to strategy
<b>Market and customer risks continued</b>			
<p><b>Loss of key customers</b></p> <p>Bodycote benefits from many long-term relationships with key customers and the damage to, or loss of, any of these relationships would be detrimental to the Group.</p>	<p><b>Stable</b></p> <p>Although the Group does not rely on any individual major customers, the loss of a key customer could adversely affect the Group's financial results and the viability of one or more of Bodycote's facilities.</p>	<ul style="list-style-type: none"> <li>■ The Group has more than 40,000 customers and there is no significant customer dependency, with the Group's top ten customers accounting for less than 16% of revenues.</li> <li>■ There is an ongoing focus on customer service and quality processes to maintain excellent relationships with customers. Key account management is in place where this is required to deliver good customer service.</li> </ul>	
<p><b>Competitor action</b></p> <p>The entry of competitors into one or more of the Group's Specialist Technologies.</p>	<p><b>Stable</b></p> <p>The erosion of market share resulting in loss of revenue and profit.</p>	<ul style="list-style-type: none"> <li>■ The close control of proprietary knowledge.</li> <li>■ Rapid increase in the scale of the Group's offerings to maintain the position as supplier of choice.</li> <li>■ A focus on customer service to ensure that satisfied customers have no cause to seek alternative suppliers.</li> </ul>	
<b>Corporate and community risks</b>			
<p><b>Safety and health</b></p> <p>The nature of Bodycote's activities presents safety and health risks.</p>	<p><b>Stable</b></p> <p>Bodycote is committed to providing a safe work environment for its employees but Bodycote's operations, if not properly managed, could have a significant impact on individual employees. Furthermore, poor safety and health practices could lead to disruption of business, financial penalties and loss of reputation.</p>	<ul style="list-style-type: none"> <li>■ Group-wide health and safety policies set by the Group Chief Executive.</li> <li>■ OHSAS 18001 and ISO 14001 compliant SHE management systems being used by Group Head of Safety, Health and Environment with support of divisional safety, health and environmental teams.</li> <li>■ Programme in place to focus on reduction of incidents which could have a high impact.</li> <li>■ Safety compliance audits at all plants at least every two years.</li> <li>■ Oversight of safety and health framework provided by the Group Risk and SHE Committee.</li> </ul>	



Risk description	Impact	Mitigation and control	Relevance to strategy
<p><b>Environment</b></p> <p>Actual or potential environmental contamination could lead to health risks, disruption of business, financial costs and loss of reputation.</p>	<p><b>Stable</b></p> <p>Bodycote is committed to providing the highest level of protection to the environment. Environmental regulators in many jurisdictions in which Bodycote operates can impose obligations on Bodycote to investigate potential contamination and remediate where required.</p>	<ul style="list-style-type: none"> <li>■ Environmental procedures and measures in place conforming to ISO 14001 (2018: 90% of plants).</li> <li>■ Environmental due diligence of businesses for acquisition.</li> <li>■ Remediation of contaminated sites or additional emission abatement as required by local legislation.</li> </ul>	
<b>Operational risks</b>			
<p><b>Service quality</b></p> <p>The Bodycote brand is reliant on the repeatable delivery of parts to agreed specification to an agreed time.</p>	<p><b>Increasing</b></p> <p>Deterioration in quality or service levels can cause serious long-term damage to Bodycote's reputation with financial consequences such as the loss of a customer and the cost of damages or litigation. Work that is released into use which is not in compliance with specification could arise as a result of system or human failure.</p> <p>Customers are tending to demand higher liabilities in respect of any quality defects or delays on Bodycote's part.</p>	<ul style="list-style-type: none"> <li>■ Bodycote has stringent quality systems in place managed by qualified staff.</li> <li>■ Quality systems and processes operated at plant level with oversight by divisional quality teams.</li> <li>■ Where necessary, plants maintain industry relevant accreditations, such as ISO 9001, Nadcap and IATF 16949.</li> <li>■ All plants subjected to internal and external quality audits and inspections at least once a year.</li> <li>■ Bodycote carefully negotiates terms and conditions associated with the supply of services to its customers, carefully managing potential liabilities.</li> </ul>	

# Principal risks and uncertainties continued

Risk description	Impact	Mitigation and control	Relevance to strategy
<b>Operational risks continued</b>			
<p><b>Major disruption at a facility</b></p> <p>Bodycote's business processes are inherently risky and there is a possibility that a major fire such as that suffered in 2018 at the Syracuse facility (USA) or utility outage could lead to closure of a facility's operation. In addition a number of sites are exposed to natural hazards, such as earthquakes, flooding and storms.</p>	<p><b>Stable</b></p> <p>Any significant incident at a site could result in the service to Bodycote's customers from the affected site being disrupted.</p>	<ul style="list-style-type: none"> <li>■ Bodycote has a global network of more than 180 facilities. These facilities create a framework to provide backup capability for affected facilities.</li> <li>■ Business continuity plans are in place for all plants. These are updated and tested annually. The Board reviewed the testing of Business Continuity plans in 2018. The fire in July 2018, which resulted in a total loss of the Group's Syracuse (USA) facility, highlighted the success of the Group's business continuity plans.</li> <li>■ Independent insurer inspections to assess hazard and business interruption risks.</li> <li>■ Insurance cover, including business interruption cover.</li> <li>■ Scheduled equipment maintenance and inspections.</li> </ul>	
<p><b>Capital projects</b></p> <p>The Group invests capital in developing existing plants as well as into Greenfield developments and acquisitions. This risk was reviewed by the Board during 2018 and additional controls will be implemented during 2019.</p>	<p><b>Increasing</b></p> <p>The Group is undertaking a higher number of capital projects. This may cause projects to be delivered late or at a higher cost than forecast. Market conditions may also change making a project less profitable than initially projected.</p>	<ul style="list-style-type: none"> <li>■ There is a well established capital investment approval process that applies to all major capital projects.</li> <li>■ Project Management frameworks are being improved and additional resource being applied to deliver projects on time and on cost.</li> <li>■ All major projects are subject to post implementation reviews.</li> </ul>	
<p><b>Information Technology projects</b></p> <p>The efficient operation of the Group relies on the smooth operation of its IT systems. During 2018, the Group completed the roll-out of the finance and purchasing modules of its ERP project. The Group continues to work on its operations module to ensure that it responds to business requirements before rolling out. The Group currently uses a range of ERP solutions to manage its operations.</p>	<p><b>Stable</b></p> <p>A significant failure of IT systems as a result of external factors, such as a cyber-attack, could disrupt service to our customers, and result in reputational loss and financial loss.</p>	<ul style="list-style-type: none"> <li>■ The Group has robust governance processes to ensure that IT projects are properly reviewed and approved to ensure that they are consistent with the Group's IT Strategy</li> <li>■ Increased focus on IT security management processes.</li> <li>■ Well protected data centres with defined disaster recovery planning and data backup procedures.</li> </ul>	

Risk description	Impact	Mitigation and control	Relevance to strategy
<b>Regulatory risks</b>			
<p><b>Regulatory and legislative compliance</b></p> <p>The global nature of Bodycote's operations means that the Group has to comply with a wide range of local and international legislative requirements, including anti-bribery and anti-competition legislation, taxation legislation, employment law and import and export controls.</p>	<p><b>Stable</b></p> <p>Failure to comply with legislation could lead to substantial financial penalties, disruption to business, diversion of management time, personal and corporate liability and loss of reputation.</p>	<ul style="list-style-type: none"> <li>■ Business processes are supported by HR policies and the Group Code of Conduct alongside training and awareness programmes.</li> <li>■ The 'Open Door Line' whistleblower facility which is managed by a third party.</li> <li>■ Engagement of local specialists to support Bodycote at local, divisional and Group level.</li> <li>■ Regular audit of the effectiveness of implemented procedures.</li> </ul>	

### Viability statement

In preparing this statement of viability, the directors have considered the prospects of the Group over the three year period immediately following the 2018 financial year. This longer term assessment process supports the Board's statements on both viability, as set out below, and going concern (on page 28). A three year period was determined as it is a reasonable period over which the business could be restructured in the event that any material changes to demand for the Group's services transpired. As a result, the Board determined that a period of longer than three years would not be meaningful for the purpose of concluding on longer term viability.

The forecast used considers metrics which enable assessment of the Group's key performance indicators (including return on capital employed, headline earnings per share and headline operating cash flow) in addition to net debt, liquidity and financing requirements.

In conducting the review of the Group's prospects the directors assessed the three year plan alongside the Group's current position, the Group's strategy and the principal risks facing the Group (all of which are detailed in the Strategic Report on pages 4 to 37). This assessment considered the impact of the principal risks on the business model and on future prospects and performance, including the possible impact of Brexit, liquidity and solvency and was mindful of the limited forward visibility that the Group has as it carries no order backlog. The directors' viability assessment included a review of the sensitivity analysis performed on the three year plan, whereby the principal risks were applied to the plan in a number of diverging scenarios. The developed scenarios were designed to be plausible, yet severe. Examples of scenarios reviewed were:

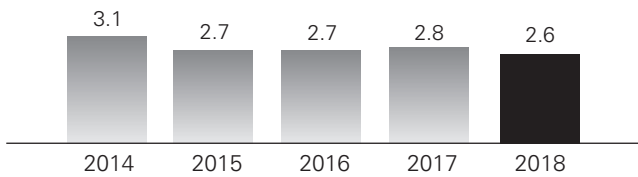
- A decrease in forecast revenue of similar magnitude to the largest year-on-year decrease suffered in the last ten years.
- A 10% decrease in revenue, debtor days and strengthening of sterling to reflect an economic downturn.

In making this viability statement the directors considered the mitigating actions that are taken by the Group in the event that the principal risks of the Company become realised. The directors also took into consideration the Group's financial position at 31 December 2018, with net cash of £36.2m, available committed facility headroom of £230m and a history of strong cash generation.

The directors have assessed the viability of the Group and, based on the procedures outlined above in addition to activities undertaken by the Board in its normal course of business, confirm that they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period to 31 December 2021.

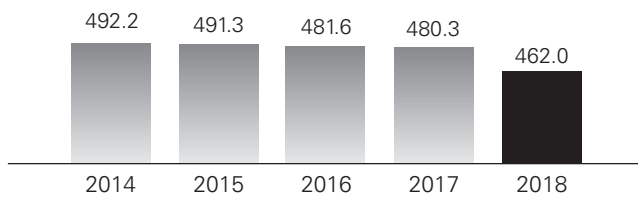
# Corporate responsibility and sustainability

## Total reportable case rate (TRC)<sup>1</sup>



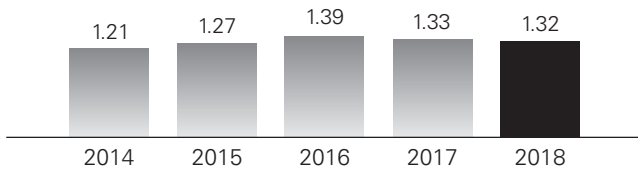
## Carbon footprint<sup>2</sup>

(tonne CO<sub>2</sub>e/£m sales normalised<sup>3</sup>)



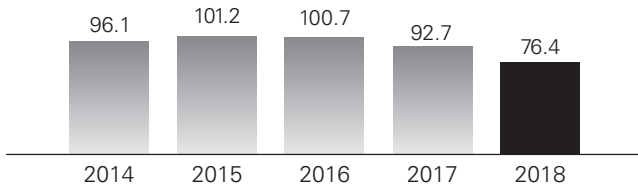
## Water consumption

(thousand m<sup>3</sup>/£m sales normalised<sup>3</sup>)



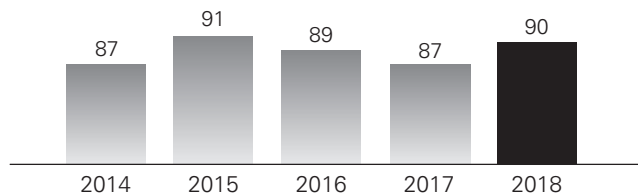
## Chlorinated solvents

(kg/£m sales normalised<sup>3</sup>)



## ISO 14001 accredited facilities

(%)



1. Total reportable case rate is defined as the number of lost time accidents x 200,000 hours (approximately 100 man years), divided by the total number of employee hours worked.

2. CO<sub>2</sub>e is carbon dioxide equivalent, which represents the CO<sub>2</sub> release due to our energy usage.

3. Normalised statistics restate prior year figures using current year IEA carbon conversion factors and current year average exchange rates.

As a Group, Bodycote is committed to acting responsibly as a good corporate citizen, to reducing the environmental impact of the Group's activities and to providing our employees with a safe working environment.

Bodycote's stakeholder model shows how its interactions on various levels contribute towards socioeconomic growth and development. These exchanges, based on mutually beneficial relationships, provide the basis for the Group's growth and sustainability, which in return provides benefits to employees, investors, customers and society communities.

## Our approach

Bodycote's objective is to create superior shareholder returns through the provision of selected thermal processing services that are highly valued by our customers. We aim to achieve this in a safe working environment, while continually seeking to minimise the impact on the environment.

Bodycote is dedicated to improving the management of corporate responsibility issues and is implementing policies and initiatives to achieve this goal. The future success and growth of the Group is intrinsically linked to our ability to ensure the Group's operations are sustainable and that we can nurture and develop our talent.

## Our people

The strength of the Group primarily rests in its people and one of the key challenges for management is to ensure availability of appropriately qualified people to support its continued growth. Bodycote is fortunate to have a competent and committed international team that is well respected in technical and business circles.

Bodycote invests in the training and development of its people both at local and Group level. The Group is committed to providing the appropriate skills and training which will allow its employees to operate effectively and safely in their roles and deliver results.

A tool to develop further understanding and skill in the area of performance management is in place and is being used globally through the management population. Through communication of clear messages coupled with skills development, the organisation aims to raise the capability of its management population in driving performance. This initiative is backed by a performance management system which supports the process.

Bodycote's employment policies are non-discriminatory, complying with all current legislation to engender equal opportunity irrespective of age, race, gender, ethnic origin, nationality, religion, health, disability, marital status, sexual preference, political or philosophical opinions or trade union membership. Harassment is not tolerated.

Female representation on our Board during 2018 was 43% (2017: 17%) and at manager level it is 26% (2017: 26%). Females represent 19% (2017: 19%) of our total workforce.

	Male	Female	Total	Male	Female	Total
Directors	4	3	7	57%	43%	100%
Managers	52	18	70	74%	26%	100%
Other staff	4,539	1,030	5,569	82%	18%	100%
	4,595	1,051	5,647	81%	19%	100%

## Culture and Values

It is not just important what we do but how we do it and how we behave in our Company. How we operate as a Group and the behaviours that we expect from all our employees are expressed in our Core Values. Our values represent Bodycote and its people and our commitment to the Company and the business.

Our Core Values are straightforward and are as follows:

**Honesty and Transparency**

We are honest and act with integrity. Trust stems from honesty and trust is at the heart of everything we engage in: our customers trust us to deliver what we say we will, our colleagues trust us to act in their best interests and our suppliers trust us to conduct business according to agreed terms. This is not something we take for granted. Bodycote lives by a culture of honest and transparent behaviour, which is at the core of all our business relationships.

**Respect and Responsibility**

We manage our business with respect, applying an ethical approach to our dealings with those we interact with. We respect our colleagues, who are all of the employees of Bodycote. Part of our respect for our colleagues is our commitment to safe and responsible behaviour and our fundamental belief that no one should come to any harm at work. We show respect for our customers, our suppliers and our competitors. We respect the communities around us and behave as responsible corporate citizens by being compliant with the laws and regulations of the countries in which we do business and by ensuring that our effect on the environment is minimal. We believe in taking ownership for, and being mindful of the impact of, our actions.

**Creating Value**

Creating value is the very essence of our business and needs to be the focus of our endeavours. We create value for our customers, our employees and our shareholders. The realities are harsh. If we do not create value for our customers then we have no reason for existence. If we do not create value for our employees there will be no one to create value for our customers. Our shareholders rightfully require that we ultimately create value for them as they are the owners of the business.

**Human rights**

Bodycote’s human rights policy is consistent with the Universal Declaration of Human Rights and the UN Global Compact’s ten principles.

We prohibit forced, compulsory and underage labour and any form of discrimination based on age, race, gender, ethnic origin, nationality, religion, health, disability, marital status, sexual preference, political or philosophical opinions or trade union membership. Appropriate mechanisms are in place to minimise the potential for any contravention of these rules.

By publicly posting our human rights policy on www.bodycote.com, stakeholders worldwide can alert us to potential breaches of the policy. Our internal systems also support compliance with our policy and we have a robust Open Door Line for employees to report alleged violations of law and/or our policies on a confidential basis and in their own language. In the jurisdictions in which we employ a majority of our employees, there are laws applicable to many of the areas dealt with in our human rights policy.

**The Modern Slavery Act**

Bodycote plc has conducted a risk assessment on our supply chain using the UK Government’s published guidance entitled ‘Transparency in Supply Chains’. Suppliers in those countries identified in Walk Free Foundation’s 2016 Global Slavery Index as being the most vulnerable to human rights issues in the supply chain have been identified for further review and audit.

We have a Code of Conduct which sets out our policy on compliance with legislation, child labour, anti-slavery and human trafficking, and conditions of employment, health and safety and the environment.

The Anti-Slavery and Human Trafficking statement was reviewed by our Board of directors in June 2018 and was published on our website. The statement will be reviewed on an annual basis.

**Customers and suppliers**

Bodycote has no significant suppliers who are wholly dependent upon the Group’s business and has no significant suppliers on which the Group is dependent upon for a substantial part of its business. Suppliers are paid in line with contractual and legal obligations.

We endeavour to respond quickly to changing customer demand,

to identify emerging needs and to improve service availability and quality. We stay close to our current and potential customers, building long-term relationships.

**Community**

Bodycote seeks to play a positive role in the local communities in which it operates by providing employment opportunities, and building goodwill and a reputation as a good neighbour and employer.

**Responsible business ethics**

The Group has a robust governance structure in place to support business ethics and a series of policies which details its commitments and standards in this area. We recognise that rules alone are not sufficient to ensure wrongdoing is avoided – a combination of rules and values is needed to help embed a healthy business culture. The Group’s approach is to set the tone of an ethical business culture from the top, demonstrating commitment to the right values and behaviours of all employees.

All Bodycote personnel are expected to apply a high ethical standard, consistent with an international UK-listed company. Directors and employees are expected to ensure that their personal interests do not at any time conflict with those of Bodycote. Shareholder employees are advised of, and comply with, the share dealing code.

Bodycote has systems in place that are designed to ensure compliance with all applicable laws and regulations, and conformity with all relevant codes of business practice. Furthermore, Bodycote does not make political donations.

With regard to competition, Bodycote aims to win business in a differentiated high-value manner. The Group does not employ unfair trading methods and it competes vigorously but fairly within the requirements of applicable laws. Employees are prohibited from either giving or receiving any inducements.

Our Open Door Policy has been translated into all languages used throughout the Group. The policy allows employees to report their concern confidentially, verbally or in writing, to an independent third party provider, ensuring anonymity.

**Responding when wrongdoing is reported**

When incidents are reported, whether through internal or external mechanisms, they are passed to the Group Head of Risk for investigation and determination of the appropriate steps to be taken for the matter to be addressed.



**Supporting employees who speak up**

When our employees do the right thing by speaking up against instances of wrongdoing, we believe it is crucial that the Group also does the right thing and ensures that there are no repercussions for their actions.

Online training courses in respect of Anti-Bribery and Competition Law have been designed and translated into the major languages used throughout the Group. All relevant employees have completed the interactive courses.

# Corporate responsibility and sustainability continued

## Operational SHE performance

Bodycote is committed to continual improvement in our safety, health and environmental performance (SHE). We are committed to complying with all local legislative requirements as a minimum and establishing consistent and robust best practices at all of our sites to deliver consistently high performance across all aspects of SHE management.

### Safety and health

The nature of the Group's operations is such that employees are inevitably exposed to hazards in the workplace. Bodycote aims to manage these hazards and thereby minimise risks to employees through the deployment of robust safety control systems and procedures, and seeks to establish these at all sites.

### Total Recordable Case rate (TRC)

Bodycote uses a global incident reporting and SHE management tool at every operational site enabling more consistent and thorough reporting of workplace injuries, near misses and unsafe conditions. In 2018, the TRC rate was 1.7.

In 2018 the number of 'Opportunities for Improvement' (OFIs) reported by employees increased by 41.7% across the Group. This improvement demonstrates stronger engagement of employees in proactively raising and rectifying safety issues. Accidents, though regrettable and unacceptable, represent learning opportunities, and is the reason that accurate reporting is an essential part of building a robust safety management system.

As our database continues to develop we are able to analyse and prioritise our safety action programmes more effectively. The most frequent cause of recordable cases is related to manual handling of parts and lifting operations and has a number of underlying causes. This is currently the subject of a Group-wide review and will be a focus for risk reduction activities over the next few years.

In 2018 additional Group SHE capital investment was made in pedestrian safety and ergonomics/manual handling improvements to reduce accident frequency, and address the severity of risk in these areas.

Reportable cases and lost time injuries are reviewed during executive management meetings and Board meetings. In addition, the executive management team reviews incidents which did not result in injury but were considered to have been serious or to have had a high potential impact. All serious incidents and high potential incidents are also reviewed by the Group SHE Committee and are cascaded within the business as appropriate to ensure that preventive actions are taken.

## Greenhouse gas emissions

	2018		2017		2017 (normalised)	
	CO <sub>2</sub> e emissions (ktCO <sub>2</sub> e)	Intensity ratio (tCO <sub>2</sub> e/£m)	CO <sub>2</sub> e emissions (ktCO <sub>2</sub> e)	Intensity ratio (tCO <sub>2</sub> e/£m)	CO <sub>2</sub> e emissions (ktCO <sub>2</sub> e)	Intensity ratio (tCO <sub>2</sub> e/£m)
Scope 1	150.6	204.7	150.3	217.9	149.9	217.1
Scope 2	189.3	257.3	189.8	275.2	181.7	263.1
Statutory total	339.9	462.0	340.1	493.1	331.7	480.3

## Environment

A proactive approach to improving energy efficiency means that Bodycote has implemented a variety of systems to reduce water and gas consumption, and to reuse heat energy. In order to lessen the impact on the environment Bodycote continues to seek ISO 14001 accreditation at all of our operational facilities.

At every stage where Bodycote is involved in the manufacturing cycle, our operational aim is to reduce the overall impact on the environment, not just in our own operations, but also those of our customers.

Bodycote operates modern, efficient equipment, which is operated around the clock so as to optimise treatment processing cycles. Without Bodycote, many companies would be using older in-house technology and running their equipment at reduced capacity, both of which drain energy resources. Working with Bodycote enables our customers to commit more easily to carbon reduction initiatives.

Bodycote also reduces the carbon footprint of our customers' activities by increasing the lifespan of their products, by improving metallurgical properties and by enhancing corrosion resistance. For example, surface treatment technology is widely used in the reclamation of damaged and worn components, offering a cost-effective and energy-efficient alternative to the need to manufacture new replacement parts. The treated parts often last up to twenty times longer than the original.

While thermal processing is an energy-intensive business, it is a vital part of the manufacturing supply chain and its use saves the energy it consumes many times over. Moreover, by effectively consolidating the heat treatment requirements of our many thousands of customers, Bodycote significantly reduces the overall required energy consumed compared with the energy that would be consumed if each customer treated their own products. In this regard, Bodycote should be viewed as an enabler to the goal of a reduction in emissions.

Scope 1 emissions are direct emissions resulting from fuel usage and the operation of facilities. Scope 2 emissions are indirect energy emissions resulting from purchased electricity, heat, steam or cooling for own use.

The financial control consolidation approach has been used to report the above data. This method aligns with the reporting scope in the financial statements. The Group collects electricity and natural gas usage information from each facility on a monthly basis. The Group then applies the International Energy Agency (IEA) published national carbon conversion factors to calculate the total tonnage of CO<sub>2</sub>e produced.

All entities and facilities under financial control are included within the disclosure. Emissions less than 1% of the Group's total CO<sub>2</sub>e relating to fugitive emissions and owned vehicles are not significant and are excluded. As such there are no significant omissions from this disclosure.

## Total Energy Consumption

	2018		
	Group Energy consumption kWh	UK Energy consumption kWh	Proportion of energy consumed in the UK
Total Energy Consumption kWh	<b>1,410,246,385</b>	<b>78,855,906</b>	<b>5.6%</b>

In 2018 the aggregate of the annual quantity of energy from activities for which the Company is responsible worldwide and the annual quantity of energy consumed resulting from the purchase of electricity, heat, steam or cooling by the Company for its own use was 1,410,246,385 kWh; the proportion of that figure that relates to energy consumed in the UK is 5.6%.

### ISO 14001 accredited facilities

Reducing the environmental impact of the Group's activities is taken very seriously. Compliance with the requirements of ISO 14001 helps to minimise the risk of adverse environmental effects at Bodycote's sites. At the end of 2018, 90% of our operating facilities had achieved ISO 14001 accreditation (2017: 87%). Operational plants which have not yet received accreditation to the standard are working towards it.

### Carbon footprint and water consumption

The absolute energy usage decreased by 0.03% and per £m sales (at constant exchange rates) decreased by 3.8%.

The total CO<sub>2</sub>e emissions per £m sales in 2018 were 466.6 Te (2017: as previously reported 493.1 Te; normalised<sup>†</sup> 480.3 Te).

The Group's total CO<sub>2</sub>e emission data is based on Scope 1 and Scope 2 emissions, as defined by the UK Government's DEFRA, and data relating to this has been calculated to include country-specific electricity conversion factors. In previous years this has been supplied by DEFRA directly. However, as of January 2017 DEFRA no longer supplies these conversion factors for non-UK companies. This has now been sourced by the Group directly from the International Energy Agency (IEA). There are some significant differences in these conversion factors. As a result all previous years have now been restated using IEA conversion factors to ensure that year-on-year comparisons are consistent.

On a normalised<sup>†</sup> basis, water usage per £m sales decreased by 0.8%. On a non-normalised basis, water usage per £m showed no change.

In 2015 our EU based operational sites reviewed their operations to ensure compliance with the Energy Efficiency Directive 2012/27/EU. This Directive is transposed into local legislation and requires

sites to monitor their energy usage and assess energy reduction opportunities which are in addition to the ongoing energy saving activities at sites. One mechanism for ensuring compliance is for sites to become certified to ISO 50001 Energy Management Systems Standard. This enables sites to measure energy usage consistently and target the most effective ways of reducing energy usage. Our sites in Germany, Austria, Denmark, the Netherlands and the UK are largely already certified and working on further energy management programmes.

Bodycote uses established systems to develop best practice at specific sites and across the wider Group.

The continued replacement of traditional lighting with LED for environmental and improved safety has resulted in further CO<sub>2</sub> reductions.

Bodycote submits data on CO<sub>2</sub> usage to the Carbon Disclosure Project, one of the leading carbon reporting and verification bodies. The Company is now standing at a 'C'.

### Chlorinated solvent use

The use of chlorinated solvents in Bodycote's thermal processing activities has been reduced in recent years as aqueous degreasing facilities have been introduced. In 2018, the normalised<sup>†</sup> solvent use showed a further decrease of 17.5% compared with the previous year.

### Cautionary statement

The Strategic report has been prepared solely to provide information to shareholders to assess how the directors have performed their duty to promote the success of the Group.

The Strategic report contains certain forward-looking statements. These statements are made by the directors in good faith based on the information available to them up to the time of their approval of this report and such statements should be treated with caution due to the inherent uncertainties, including both economic and business risk factors, underlying any such forward-looking information.

### Approval

The Group Strategic report of Bodycote plc was approved by the Board of directors and signed on its behalf by:

#### S.C. Harris

Group Chief Executive  
8 March 2019

\* Statutory carbon reporting disclosures required by Companies Act 2006.

† Normalised statistics restate prior year emissions using current year IEA carbon conversion factors and current year average exchange rates.

†† Emissions per £m of turnover.

# Board of Directors

## Executive Directors



**Stephen Harris**  
GROUP CHIEF EXECUTIVE

APPOINTED:  
November 2008, and Executive from January 2009. E

### External roles

Non-Executive Director, Chair of Sustainable Development Committee and Chair of Social and Ethics Committee for Mondi plc.

### Past roles

Spent his early career in engineering with Courtaulds plc and then moved to the USA to join APV Inc from 1984 until 1995, where he held several senior management positions. He was appointed to the Board of Powell Duffryn plc as an Executive Director in 1995 and then went on to join Spectris plc as an Executive Director from 2003 to 2008. He was also a Non-Executive Director of Brixton plc from 2006 to 2009.

### Qualifications

Chartered Engineer, graduated from Cambridge University, Master's degree in business administration from the University of Chicago, Booth School of Business.

### Skills and experience

- Management
- Leadership
- Mergers and acquisitions
- International operations
- Emerging markets
- Engineering
- Service industry
- Capital intensive industry

## Non-Executive Directors



**Dominique Yates**  
CHIEF FINANCIAL OFFICER

APPOINTED:  
November 2016 E

### External roles

None.

### Past roles

Held various senior positions in Imperial Tobacco Group plc followed by Chief Financial Officer positions at Symrise AG, LM Windpower and most recently at Regus plc from 2011 to 2015.

### Qualifications

Chartered Accountant, graduated from Bristol University in Economics and Accounting.

### Skills and experience

- Leadership
- International operations
- Mergers and acquisitions
- Emerging markets
- Current financial experience
- Service industry



**Anne Quinn CBE**  
CHAIR

APPOINTED:  
January 2018 N

### External roles

None.

### Past roles

Worked in various roles for NZ Forest Products Ltd, followed by management consultancy with Resource Planning Associates, a management position with Standard Oil and various senior management roles with BP plc from 1987 to 2007. Managing Director of Riverstone Holdings LLC from 2008 to 2009. Non-Executive Director of BOC Group plc from 2004 to 2006, Non-Executive Director and Remuneration Committee Chair as well as Senior Independent Director of Mondi plc from 2007 to 2017 and Non-Executive Director and Remuneration Committee Chair of Smiths Group plc from 2009 to 2018.

### Qualifications

B.Com University of Auckland and MSc Management Sciences, Massachusetts Institute of Technology.

### Skills and experience

- International operations
- Emerging markets
- Mergers and acquisitions
- Management
- Leadership
- Manufacturing
- Capital intensive industry
- Managing Director



**Ian Duncan**  
SENIOR INDEPENDENT DIRECTOR

APPOINTED:  
November 2014 A R N

### External roles

Non-Executive Director and Chairman of the audit committee of Babcock International Group plc since 2010 and a Non-Executive Director and Chairman of the audit committee of SIG plc from 2017.

### Past roles

Worked on a variety of audits with Deloitte & Touche, followed by four years with Dresdner Kleinwort Wasserstein. From 1990 to 1992 he worked for Lloyds Bank plc and then switched to British Nuclear Fuels plc from 1993 to 2006. In 2006 he took on the role of Group Finance Director with Royal Mail Holdings plc leaving in 2010. He was Non-Executive Director of Fiberweb plc during 2013, Mouchel Group from 2013 to 2015 and WANdisco plc from 2012 to 2016.

### Qualifications

Chartered Accountant, qualified with Deloitte & Touche after graduating from University of Oxford.

### Skills and experience

- International operations
- Current financial experience
- Supply chain and logistics
- Mergers and acquisitions
- Service industry





**Eva Lindqvist**  
NON-EXECUTIVE DIRECTOR

APPOINTED: June 2012 (R) (A) (N)

**External roles**

Non-Executive Director of Sweco AB since 2013, Tele 2 AB (merged with ComHem Holding AB in November 2018) from 2014 and Keller Group plc since 2017.

**Past roles**

Began her career in various positions with Ericsson working in Continental Europe, North America and Asia from 1981 to 1990 followed by director roles with Ericsson from 1993 to 1999. Joined Teliasonera in 2000 as Senior Vice President moving to Xelerated initially as Chairperson and later as Chief Executive from 2007 to 2011. Non-Executive Director of Transmode Holdings AB from 2007 to 2013, Blekinge Institute of Technology from 2010 to 2013, Tieto Corporation from 2010 to 2016, Assa Abloy from 2008 to 2018, Caverion Oy from 2013 to 2018, Alimak Holding from 2015 to 2018, Micronic Mydata AB from 2013 to 2016, and Mr Green & Co AB from 2016 to February 2019.

**Qualifications**

Engineer, graduated with a Masters from Linköping Institute of Technology, Diploma in Marketing from IHM Business School and MBA Financial Analysis from University of Melbourne.

**Skills and experience**

- International operations
- Manufacturing
- Engineering
- Technology
- Mergers and acquisitions
- Service industry
- Sales and marketing



**Patrick Larmon**  
NON-EXECUTIVE DIRECTOR

APPOINTED: September 2016 (A) (R) (N)

**External roles**

Non-Executive Director of Huttig Building Products Inc., a NASDAQ listed international distributor of construction products since 2015.

**Past roles**

Was Executive Vice President and owner of Packaging Products Corporation until 1990 when the company was acquired by Bunzl plc. Held various senior management positions for over 13 years before becoming President of Bunzl's North America business in 2003, then Chief Executive Officer, North America, of Bunzl plc in 2004, joining the Bunzl plc board in 2005. Retired from Bunzl plc on 31 December 2018.

**Qualifications**

Graduated from Illinois Benedictine University (major Economics & Business Economics) followed by achieving Certified Public Accountant, followed by an MBA from Loyola University of Chicago and a Masters of International Business from St. Louis University.

**Skills and experience**

- International operations
- Mergers and acquisitions
- Service industry
- Manufacturing
- Distribution
- Sales and marketing
- Chief Executive Officer



**Lili Chahbazi**  
NON-EXECUTIVE DIRECTOR

APPOINTED: January 2018 (A) (R) (N)

**External roles**

Strategy consultant and since 2008 a global partner in the London office of Bain & Company.

**Past roles**

Lili began her career as an actuary before joining Bain & Company.

**Qualifications**

Graduated with a BSc in Mathematics from Concordia University, Montreal followed by an MBA from INSEAD, Fontainebleau. Associate of the Society of Actuaries.

**Skills and experience**

- Strategy and consultancy
- International operations
- Mergers and acquisitions
- Oil & gas industry
- Business services industry
- Oilfield services and engineering services industries
- Transport industry



**Ute Ball**  
GROUP COMPANY SECRETARY

**Registered office**

Springwood Court  
Springwood Close  
Tytherington Business Park  
Macclesfield  
Cheshire  
SK10 2XF

Tel: +44 1625 505300  
Fax: +44 1625 505313

Registered Number  
519057 England and Wales.

# Corporate governance statement

## Chair's message

Dear Shareholders

On behalf of the Board, I am pleased to present Bodycote's Corporate Governance Statement for 2018.

The Board is mindful of the 2018 corporate governance code and changes in legislation introduced during the year and that are intended to encourage responsible corporate behaviour. We understand that these changes are aimed at ensuring that in growing a business for the long-term interest of its shareholders, a board is mindful of the company's broader purpose and its responsibilities to a broader stakeholder group. These changes also highlight the importance of ensuring that the Company's purpose, strategy, and values are fully aligned and clearly articulated. The Annual Report provides some information on stakeholder and stakeholder engagement and we expect to report more fully on these matters in the 2019 Annual Report.

An Employee Advisory Committee chaired by one of our Non-Executive directors, Patrick Larmon, was introduced during 2018 and the first meeting has taken place. A variety of topics were raised by employees at the meeting and these were presented directly to the Board. A number of these are now in progress to be addressed.

The main Group-wide governance documents are our Core Values and the Code of Conduct, which set out the values and standards that we expect of our employees. These documents, together with our policies, govern how we conduct our business and set the standards that drive performance. Compliance training helps to enforce this. Board oversight, reviews and audits form part of the monitoring and supervision process. Risk processes are embedded and reviewed on an ongoing basis across the business. The important governance developments at Bodycote over the last year are detailed in the governance reporting section below.

We are committed to conducting business responsibly. By maintaining high standards of corporate governance we enhance performance underpinned by our business model. Our approach to governance is set by the Board and our Executive Committee ensures that the approach is effectively implemented across the business. Effective and robust governance remains central to the ongoing success of the Group.

My ambitions for the composition of the Board are to maintain and, where applicable, broaden the range of expertise, experience and diversity. The Board continues to ensure that effective succession plans are in place.

I encourage all shareholders to attend the AGM, which will be held at our Macclesfield head office on 24 May 2019. This event provides an excellent opportunity to meet the executive and independent Non-Executive directors.

**A.C. Quinn**

Chair

## Board performance

### Key activities

#### Strategic Leadership

- Regularly discussing strategy at Board meetings during the year
- Receiving presentations from operational management on future strategic opportunities
- Considering potential acquisition opportunities and other strategic initiatives
- Considering the proposal to open new Specialist Technologies facilities in the United States
- Considering the 15-year contract with Rolls-Royce
- Considering the new heat treatment facility in Rotherham to support the aerospace and power generation markets

#### People and Succession

- Considering proposals on succession planning, when required, for the Board
- Reviewing proposals on senior executive succession planning
- Considering the talent management programme and the need to develop the managers and executives for the future
- Reviewing the structure, size, composition and diversity of both the Board and its Committees (supported by the Nomination Committee)
- Approving further three year terms as Non-Executive Directors for Patrick Larmon and Ian Duncan
- Induction programme for new Non-Executive Director and the Chair

#### Governance and Risk

- Reviewing the three year forecast and other factors to support the Viability Statement
- Reviewing Board and Committee effectiveness and directors' conflicts of interest
- Reviewing terms of reference of all Committees
- Reviewing Health, Safety and Environmental updates at each meeting
- Reviewing principal financial and non-financial risks (supported by the Audit Committee)
- Reviewing new corporate governance code and related legislation

#### Performance Monitoring

- Approving the Group's strategy and budget
- Approving the Group's tax and dividend strategy
- Recommending the 2018 final dividend, the 2018 special dividend and the 2018 interim dividend
- Reviewing and approving the Group's annual budget, interim results and Annual Report
- Considering whether the Annual Report and Accounts are fair, balanced and understandable
- Considering monthly operational reports from the Chief Executive and Chief Financial Officer
- Reviewing reports from the Chairs of the Audit, Nomination, Remuneration and Finance Committees
- Approving capital expenditure proposals in excess of £4m

## Operation of the Code

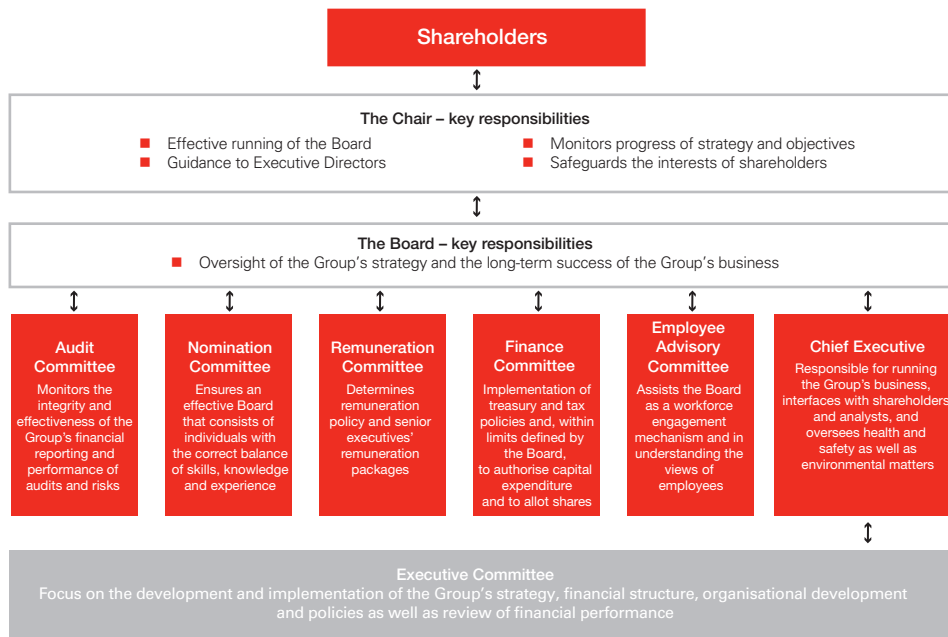
Taken together with the Report of the Audit Committee, the Report of the Nomination Committee and the Board report on remuneration presented on pages 52 to 77, this statement explains how Bodycote has applied the principles of good corporate governance as set out in the Code.

## Governance reporting

### Leadership

The Board is responsible to shareholders for good corporate governance, setting the Group's strategic objectives, values and standards, and ensuring the necessary resources are in place to achieve the objectives.

The Board met on eight occasions during 2018, including a specific meeting to review the Group's long-term strategy. The Board of directors comprises seven members, of whom five are Non-Executive directors and two are executive directors, led by the Group's part-time Non-Executive Chair, A.C. Quinn, who also chairs the Nomination Committee. The Group Chief Executive is S.C. Harris and the Senior Independent Non-Executive Director is I.B. Duncan, who also chairs the Audit Committee. E. Lindqvist is Chair of the Remuneration Committee. P. Larmon and L. Chahbazi are Non-Executive Directors. Brief biographical details of all directors are given on pages 38 to 39. During the year the Board visited a number of UK and overseas facilities, including sites in Germany and the USA. Such events involved meetings with local management and the workforce to understand more clearly technical and operational performance in countries where Bodycote has a significant presence.



The SHE and Risk Committee reports to the Executive Committee.

In order that necessary actions can be taken promptly, a finance sub-committee, comprising the Chair, the Senior Independent Director, the Group Chief Executive and the Chief Financial Officer operates between the dates of scheduled Board meetings and is authorised to make decisions, within limits defined by the Board, in respect of certain finance, treasury, tax or investment matters.

# Corporate governance statement continued

## Individual roles of the Board

### Chair

- leadership and governance of the Board and chairs the Nomination Committee
- Board effectiveness
- ensures members receive accurate, timely and clear information on Board issues
- ensures, together with the Group Company Secretary, comprehensive induction of new directors
- sets Board agenda, style and tone of Board discussions
- ensures effective communication with shareholders

### Group Chief Executive

- overall responsibility and leadership of the Group performance
- stewardship of Group assets
- plans and executes objectives and strategies
- maintains a close working relationship with the Chair, ensuring effective dialogue with investors and stakeholders
- ensures the leadership and development frameworks are developed to generate a positive pipeline for future opportunities for the Group
- has overall responsibility for the Group's sustainability performance
- communicates the vision and values of the Group
- manages the senior management team

### Chief Financial Officer

- maintains strong financial management and implements effective financial controls
- provides financial and commercial decision leadership, vision and support
- ensures the appropriateness of risk management systems
- oversees all aspects of accounting/finance operations including accounting policies and integrity of financial data and external financial reporting
- responsible for corporate finance functions, financial planning and budget management
- supports and advises the senior management team
- leads the development of investor relations strategy and communications

### Senior Independent Director

- acts as a sounding board for the Chair
- serves as an intermediary for other directors
- is available to meet shareholders if they have concerns which they have not been able to resolve through the normal channels
- conducts an annual review of the performance of the Chair and convenes a meeting of the Non-Executive directors to discuss the same

### Non-Executive Directors

- provide constructive challenge
- help develop strategy
- ensure financial controls and systems of risk management are robust and defensible
- determine appropriate levels of remuneration for the executive directors
- monitor reporting of performance
- scrutinise performance of management
- are available to meet with major shareholders

### Group Company Secretary

- secretary to the Board and its committees
- ensures efficient information flows within the Board and its committees and between senior management and Non-Executive directors
- facilitates induction of new directors and assists with training and development needs as required
- regularly updates the Board on corporate governance matters, legislative changes and regulatory regimes affecting the Group
- ensures compliance with Board procedures
- co-ordinates external Board evaluation and conducts internal Board evaluation

### Board diversity

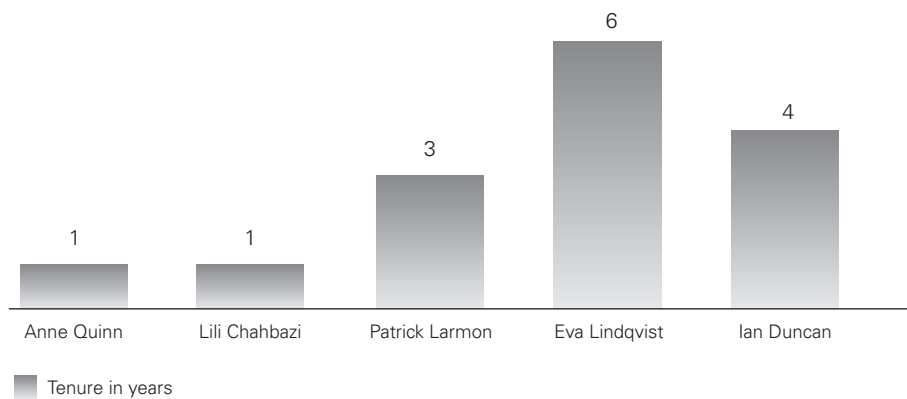
Bodycote is a global business with operations in 23 countries and diversity is an integral part of how we do business. The Nomination Committee considers diversity when making appointments to the Board, taking into account relevant skills, experience, knowledge, personality, ethnicity and gender. Our prime responsibility, however, is the strength of the Board and our overriding aim in any new appointment must always be to select the best candidate. The Nominations Committee also considers capability and capacity to commit the necessary time to the role in its recommendation to the Board. The intention is to appoint the most suitable qualified candidate to complement and balance the current skills, knowledge and experience of the Board and who will be best able to help lead the Company in its long-term strategy. The Nomination Committee is advised by international search companies, who have been briefed on our diversity policy and are required to reflect the policy in the long list submitted to the Committee.

We appointed A.C. Quinn on 1 January 2018 as part of our Board refreshment replacing A.M. Thomson, who retired on 31 December 2017 as Chairman of the Board. L. Chahbazi was appointed Non-Executive director effective 1 January 2018. The Board currently comprises two executive directors, four Non-Executive directors and a Non-Executive Chair.

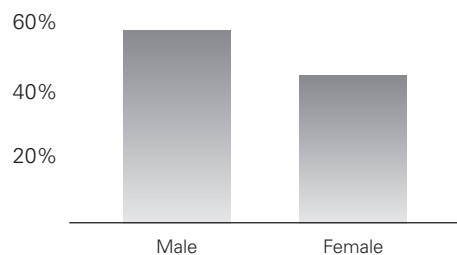
As of 2018 female representation on our Board is 43% (2017: 17%). At manager level it is 26% (2017: 26%). Females represent 19% (2017: 19%) of our total workforce. Whilst we are above the 33% by 2020 voluntary target recommended by the Hampton-Alexander review, we continue to believe it is difficult to set targets or timescales for increasing the proportion of women, or any other minority group, on our Board and do not propose to do so. We will increase female and/or other minority representation on the Board if appropriate candidates are available when Board vacancies arise.

The Corporate responsibility and sustainability report contains further details regarding the male and female representation within the Group, including Board representation.

### Board by Tenure



### Board by Gender



### Board evaluation

The Board has undertaken its third external Board Evaluation during 2018. Following a review of proposals from external providers, the Board appointed Independent Audit to facilitate a review of its effectiveness. The review was undertaken by Catherine Stalker and Veronica Haidar. Neither of them or Independent Audit have any connection with Bodycote. The main steps of the process were:

- Document review – one set of Board and Committee papers to understand the Board in context and to assess the way information is communicated
- Interviews – with all Board members, the Group Company Secretary and the Group Head of Risk
- Observation – the Board and a Committee were observed in action to see how information is used, the style of discussions and how the Board and management work together.
- Report and presentation – the draft report was discussed with the Chair prior to its finalisation and the findings presented at the December Board meeting

# Corporate governance statement continued

The review looked at boardroom dynamics, strategic focus, corporate responsibility, risk oversight, people and culture, secretariat, organisation and chairing of Board and Committee meetings.

The results of the evaluation were considered by the Board at its meeting in December 2018. The directors discussed the recommendations and considered how they will take them forward. Some of the topics touched were succession planning, longer-term strategy for safety as well as minor changes to meeting organisation. The Board is considered to not only be operating well in its oversight role, but also providing valuable input into the strategic development of the Group. NEDs and Executive Directors engage in a cooperative and constructive relationship and the atmosphere in the boardroom is collegiate with a strong sense of shared values and transparency in discussions. The overall conclusion is that the Board and committees are well chaired and high governance standards have been adopted. It is apparent that the Executive is being strongly challenged by the non-executives when appropriate.

As in previous years, the Chair has assessed the performance of each Board member by conducting individual interviews and we can confirm that all directors continue to perform effectively and demonstrate commitment to their roles.

The Executive Directors Messrs S.C. Harris and D.Yates will be appraised in March 2019.

## Overboarding





















At our AGM in 2017, Bodycote received a high number of votes against the re-election of Eva Lindqvist. Eva has reviewed her directorships and during 2018 these were reduced to five including Bodycote.

## Independence of Non-Executive directors

The Board considers that P. Larmon, E. Lindqvist, I.B. Duncan and L. Chahbazi are all independent for the purposes of the Code. The Chair was considered independent upon appointment.

## Commitment

Attendance of directors at regular scheduled meetings of the Board and its Committees is shown in the table below:

Meetings held during the year	Board	Audit Committee	Nomination Committee	Remuneration Committee
	8	6	2	6
Executive Directors	Meetings attended	Meetings attended	Meetings attended	Meetings attended
Anne C. Quinn		n/a		n/a
Stephen Harris		n/a	n/a	n/a
Dominique Yates		n/a	n/a	n/a
Non-Executive directors	Meetings attended	Meetings attended	Meetings attended	Meetings attended
Eva Lindqvist				
Ian Duncan				
Patrick Larmon				
Lili Chahbazi				

All directors attended the maximum number of Board, Audit and Nomination Committee meetings that they were scheduled to attend. Non-members A.C. Quinn, S.C. Harris, D.Yates attended by invitation some parts of the meetings of the Audit, Nomination and Remuneration Committees.

## Proposals for re-election

The Board decided, in line with the Code, that all directors will retire annually and, other than in the case of any director who has decided to stand down from the Board, will offer themselves for re-election at the AGM. Accordingly, A.C. Quinn, S.C. Harris, E. Lindqvist, P. Larmon, I.B. Duncan, D.Yates and L. Chahbazi will stand for re-election at the AGM in May 2019.

The Board recommends to shareholders that they re-elect all the directors. In accordance with the recommendations of the Code, Board members will serve for a period of six years which may be extended in certain circumstances.

The performance of each director was evaluated as indicated above and the Board confirms in respect of each that their performance continues to be effective and that each continues to demonstrate commitment to his or her respective role.

## Induction

All new directors are subject to a tailored induction programme covering a diverse range of topics including trading, investor relations, organisational and legal matters as well as visits to operational sites. They also meet all other directors and senior executives. This facilitates their understanding of the Group and the key drivers of business performance.

## Training

The Board receives training via ad hoc presentations and papers from advisers and the Group Company Secretary. External periodic training on important topics takes place and during the year the directors received training on the new requirements in the 2018 Corporate Governance Code, updates on IA, ISS and other voting guidelines, GDPR, The Modern Slavery Act, gender diversity, guidance on strategic report, an economist briefing and other areas of focus for 2018/19. Other opportunities for ongoing development and support are:

- a programme of plant/site visits throughout the year;
- reviews with the Chair to identify any training and development needs;
- advice on governance, relevant legislative changes affecting the business or their duties from the Company Secretary;
- access to independent professional advice at the Company's expense; and
- participation in the training and guidance programme for boards and directors offered at the Deloitte Academy.

## Succession planning

Succession planning ensures that appropriate senior executive leadership resources are in place to achieve Bodycote's strategic objectives. The plans are reviewed annually by the Nomination Committee.

The Board further develops its knowledge and gains greater visibility of executive talent and management succession by visiting the Group's sites and meeting with key talent and senior executives.

## Core values

The Board acknowledges its responsibility for determining and maintaining the Group's values and ensures these are reflected in the business practices. This is monitored by the Board at regular intervals. Further details are available on page 34.

## Compliance reporting

In respect of the financial year 2018, Bodycote's obligation under the Disclosure and Transparency Rules is to prepare a corporate governance statement with reference to the UK Corporate Governance Code issued by the FRC in April 2016 ('the Code').

In respect of the year ended 31 December 2018, Bodycote has complied with the provisions of the Code with the exception of provisions E.1.1. Regarding E.1.1, the Board has, in recent years, taken the view that generally it is the responsibility of the Group Chief Executive and the Chief Financial Officer to manage relationships with institutional investors. The Chair also meets institutional investors to discuss overall strategy, governance and any concerns that shareholders may have. Only where these more usual channels of communication have failed would the Board expect the Senior Independent Non-Executive Director (SID) or other Non-Executive directors to become involved, notwithstanding that the Code specifies attendance of the SID at meetings with major shareholders. The SID has contacted major shareholders and offered to facilitate meetings with them should they have any concerns they wish to discuss. Regular feedback from the Group's advisers on investor meetings and results presentations is circulated to all directors. During the year the Chair met with shareholders to discuss governance matters.

Apart from these distinct areas, Bodycote was in compliance with the provisions of the 2016 Code throughout 2018.

Matters reserved for the Board were reviewed during the year and updated where required. Certain defined powers and issues reserved for the Board to decide are, *inter alia*:

- Strategy;
- Approval of financial statements and circulars;
- Capital projects, acquisitions and disposals;
- Annual budgets;
- Directors' appointments, service agreements, remuneration and succession planning; Policies for financial statements, treasury, safety, health and environment, donations;
- Committees' terms of reference;
- Board and committee Chairs and membership;
- Investments;
- Equity and bank financing;
- Internal control and risk management;
- Corporate governance;
- Key external and internal appointments; and
- Employee share incentives and pension arrangements.

In advance of Board meetings, directors are supplied with up-to-date information regarding the trading performance of each operating

# Corporate governance statement continued

division and subdivision, in addition to the Group's overall financial position and its achievement against prior year results, budgets and forecasts. They are also supplied with the latest available information on safety, health and environmental and risk management issues and details of the safety and health performance of the Group, and each division, in terms of severity and frequency rates for accidents at work. Senior management from across the Group and advisers attend some of the meetings to provide updates. The exposure to members of senior management from across the Group helps enhance the Board's understanding of the business, the implementation of strategy and the changing dynamics of the markets in which the Group operates.

Where required, a director may seek independent professional advice, the cost of which is reimbursed by the Group. All directors have access to the Group Company Secretary and they may also address specific issues with the SID. In accordance with the Articles of Association, all newly appointed directors must submit themselves for election. All directors stand for yearly re-election. Non-executive directors, including the Chair, are appointed for fixed terms not exceeding three years from the date of first election by shareholders, after which the appointment may be extended by mutual agreement. A statement of the directors' responsibilities is set out on page 78. The Board also operates four committees. These are the Nomination Committee, the Remuneration Committee, the Audit Committee and the Finance Committee. All Non-Executive directors serve on each Board Committee.

## Engagement with shareholders

The Group Chief Executive and Chief Financial Officer regularly talk with and meet institutional investors, both individually and collectively, and this has enabled institutional investors to increase their understanding of the Group's strategy and operating performance. In addition, internet users are able to view up-to-date news on the Group and its share price via the Bodycote website at [www.bodycote.com](http://www.bodycote.com). Users of the website can access recent announcements and copies of results presentations and can enrol to hear live presentations. On a regular basis, Bodycote's financial advisers, corporate brokers and financial public relations consultants provide the directors with opinion surveys from analysts and investing institutions following visits and meetings with the Group Chief Executive and Chief Financial Officer. The Chair and SID are available to discuss any issues not resolved by the Group Chief Executive and Chief Financial Officer. On specific issues, such as the review of remuneration packages, the Group has sought, and will continue to seek, the views of leading investors.

## Pre-emption rights

In line with best practice provisions in the Pre-Emption Group Statement of Principles, the Board confirms that it does not intend to issue more than 7.5% of the issued share capital of the Group on a non pre-emptive basis in any rolling three-year period.

## Internal control and risk management

The Board recognises that it is responsible for the Group's system of internal control and risk management. The system in place has been developed to meet the guidance contained in the Financial Reporting Council's 'Guidance on Risk Management, Internal Control and Related Financial Business Reporting'. The system has been designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss.

The Board has established a continuous process for identifying, evaluating and managing the Group's significant risks, including risks arising out of Bodycote's corporate and social engagement. The Board's monitoring covers all significant strategic, financial, operational and compliance risks. It is based principally on reviewing reports from management and from Internal Audit (IA) to consider whether any significant weaknesses are promptly remedied or indicate a need for more extensive monitoring. The Audit Committee assists the Board in discharging these review responsibilities.

The Board believes that the Group maintains an effective system of internal controls and, in the view of the Board, no significant deficiencies have been identified in the system. The system was in operation throughout 2018 and continues to operate up to the date of the approval of this report. Key elements of the Group's system of internal control are as follows:

- The Group prepares a comprehensive annual budget which is closely monitored and updated quarterly. The Group's authority matrix was reviewed and updated during 2018 and this clearly sets out authority limits for those with delegated responsibility and specifies what can only be decided with central approval.
- The Board, with the assistance of EY, who provide co-sourced IA services, monitors the Group's internal control system. IA reviews are conducted on the basis of a risk based plan approved annually by the Audit Committee. This includes risk based visits to each division, shared service centres and facility. The findings and recommendations from IA are reported on a regular basis to the Executive and Audit Committees.
- An annual internal control self-assessment, with management certification, is undertaken by every Bodycote facility. The assessment covers the effectiveness of key financial and compliance controls and was revised at the start of 2018 to include selected operational controls. The results are validated by IA through spot checks and are reported to the Executive and Audit Committees.
- Group Core Values and Group Policies (including the Code of Conduct, Group Authority Matrix and Finance Policies) are documented and are available to all employees via the Group's intranet system.



- The Chief Financial Officer, Group Financial Controller, President and Vice President of Finance for each division sign a letter of representation annually. This is to confirm the adequacy of their systems of internal controls, their compliance with Group Core Values and Group Policies, relevant laws and regulations, and that they have reported any control weaknesses and actual, or attempted, frauds or thefts through the Group's assurance processes.
- A Group-wide risk register and assurance map is maintained throughout the year to identify the Group's key strategic and operational risks. Any changes to these risks during the year are promptly reported to the Executive Committee and the Board.

During 2018, in compliance with provision C.2.1 of the Code, management performed a specific assessment of its risk management processes for the purpose of this Annual Report. Management's assessment, which has been reviewed by the Audit Committee and the Board, included a review of the Group's key strategic and operational risks. The review was based on work performed by the Group Head of Risk and the Group's Risk and SHE Committee (by means of workshops, interviews, investigations and by reviewing departmental or divisional risk registers). These risks have been reviewed throughout the year and no new risks have been added in 2018. The two risks added in 2017, Environmental and Capital Projects, have been subject to specific Board reviews during 2018. Further information regarding the ways in which the principal business risks and uncertainties affecting the Group are managed is shown on pages 29 to 33.

By order of the Board:

**U.S. Ball**  
Group Company Secretary  
8 March 2019

Springwood Court  
Springwood Close  
Tytherington Business Park  
Macclesfield  
Cheshire  
SK10 2XF

# Directors' report

The directors are pleased to submit their report and the audited financial statements for the year ended 31 December 2018.

The Chair's statement, the Chief Executive's review, the Chief Financial Officer's report and all the information contained on pages 20 to 28 together comprise the Directors' report for the year ended 31 December 2018.

## Strategic report

The Strategic report is provided on pages 4 to 37 of this Annual Report. This is a review of the development of the Group's businesses, the financial performance during the year ended 31 December 2018, key performance indicators and a description of the principal risks and uncertainties facing the Group. The Strategic report has been prepared solely to assist the shareholders in assessing the Group's strategies and the potential of those strategies. It should not be relied on by any other party for any other purpose. Forward-looking statements have been made by the directors in good faith using information available up to the date of this report and such statements should be regarded with caution because of the inherent uncertainties in economic trends and business risks. Since the end of the financial year no important events affecting the business of the Group have occurred.

## Dividends

The Board has recommended a final dividend of 13.3p (2017: 12.1p) bringing the total ordinary dividend to 19.0p per share (2017: 17.4p). If approved by shareholders, the final dividend of 13.3p per share will be paid on 7 June 2019 to all shareholders on the register at the close of business on 23 April 2019. A special dividend of 20.0p has also been proposed and will be subject to shareholder approval. If approved, it will be paid on 7 June 2019.

## Share capital

The Company's issued ordinary share capital as at 31 December 2018 was £33.1m. No shares were issued during the year. At the AGM on 30 May 2018 the shareholders authorised the Company to purchase up to 22,046,468 of its own shares. This authority expires at the conclusion of the forthcoming AGM to be held on 24 May 2019, at which time a further authority will be sought from shareholders.

## Capital structure

Details of the issued share capital are shown in note 23. The Company has one class of ordinary shares, which carries no right to fixed income. Each share carries the right to one vote at general meetings of the Company. There are no specific restrictions on the size of a holding nor on the transfer of shares, both of which are governed by the general provisions of the Articles of Association and prevailing legislation. The directors are not aware of any agreements between holders of the Company's shares that may result in restrictions on the transfer of securities or on voting rights. Details of employee share schemes are set out in note 27 and shares held by the Bodycote Employee Benefit Trust abstain from voting and waive dividend rights. No person has any special rights of control over the Company's share capital and all issued shares are fully paid. The appointment and replacement of directors is governed by the Company's Articles of Association, the UK Corporate Governance Code, the Companies Act and related legislation. The Articles of Association may be amended by a special resolution of shareholders. The powers of the directors are described in the Corporate governance statement on page 40. Under the Articles of Association the Company has authority to issue ordinary shares with a nominal value of £11,023,234.

There are also a number of other agreements that take effect, alter, crystallise or terminate upon a change of control of the Company following a takeover bid such as commercial contracts, bank loan agreements, property lease agreements, employment contracts and employee share plans. None of these are considered to be significant in terms of their likely impact on the business of the Group as a whole, and the directors are not aware of any agreements between the Company and themselves or employees that provide for compensation for loss of office or employment that occurs because of a takeover bid except where specifically mentioned in this report.

## Directors

The current directors and their biographical details are listed on page 38 to 39 and all served throughout the year. A.C. Quinn commenced as Chair as of 1 January 2018. A further Non-Executive Director, L. Chahbazi was appointed effective 1 January 2018. In line with the UK Corporate Governance Code, all directors retired at the AGM in 2018 and stood for re-election by the shareholders. Going forward all directors will retire at the AGM and will stand for re-election by the shareholders, if they wish to continue to serve as directors of the Company. Accordingly, those directors retiring and offering themselves for re-election at the 2019 AGM are A.C. Quinn, S.C. Harris, D. Yates, I.B. Duncan, E. Lindqvist, P. Larmon and L. Chahbazi. The service agreements for Messrs S.C. Harris and D. Yates are terminable by 12 months' notice. The remaining directors do not have a service agreement with the Company and their appointments are terminable by six months' notice.

## Directors' interests in contracts and shares

Details of the executive directors' service contracts and details of the directors' interests in the Company's shares and share incentive plans are shown in the Board report on remuneration on pages 56 to 77. No director has had any dealings in any shares or options in the Company since 31 December 2018. Qualifying third party indemnity provision (as defined by section 234 of the Companies Act 2006) has remained in force for the directors for the year ended 31 December 2018 and, as at the date of this report, remains in force for the benefit of the current directors in relation to certain losses and liabilities which they may incur (or have incurred) to third parties in the course of their duties. Apart from these exceptions, none of the directors had a material interest in any contract of significance in relation to the Company and its subsidiaries at any time during the financial year.

## Potential conflicts of interest

During 2008 the duties owed by directors to a company were codified and extended by the Companies Act 2006 so that directors not only had to declare actual conflicts of interests in transactions as they arose, but also had a duty to avoid such conflicts whether real or potential. Potential conflicts of interest could arise where a single director owes a fiduciary duty to more than one organisation (a 'Situational Conflict') which typically will be the case where a director holds directorships in more than one company. In order to ensure that each director was complying with the duties, each director provided the Company with a formal declaration to disclose what Situational Conflicts affected him or her. The Board reviewed the declarations and approved the existence of each declared Situational Conflict up until September 2019 and permitted each affected director to attend and vote at Bodycote directors' meetings, on the basis that each such director continued to keep Bodycote's information confidential, and provided overall that such authorisation remained appropriate and in the interests of shareholders. Where such authorisation becomes inappropriate or not in the interests of Bodycote shareholders, the Chair or the Nomination Committee can revoke an authorisation. No such revocations have been made.

## Employment

The Group recognises the value that can be added to its future profitability and strength by the efforts of employees. The commitment of employees to excel is key to the Group's continued success. Through their attendance at or participation in strategy, production, safety and health meetings at site level, employees are kept up to date with the performance and progress of the Group, the contribution to the Group made by their site, and are advised of safety and health issues. Under the Group's Open Door Line employees' concerns can be voiced over the phone on an anonymous basis in the local language. Approximately 3,600 Bodycote employees are connected to the Bodycote intranet, which improves knowledge of Group activities, and assists greatly with technology exchange and co-ordination. It is the Group's policy to give full and fair consideration to applications for employment from disabled persons, having regard to their particular aptitudes and abilities, and to encourage the training and career development of all personnel employed by the Group, including disabled persons. Should an employee become disabled, the Group, where practicable, will seek to continue the employment and arrange appropriate training. An equal opportunities policy is in operation in the Group.

## Greenhouse gas emissions

Details of greenhouse gas emissions are included within the Corporate responsibility and sustainability section of this report.

## Donations

There were no political contributions in 2017 or 2018.

## Shareholders

An analysis of the Company's shareholders and the shares in issue at 25 February 2019 together with details of the interests of major shareholders in voting shares notified to the Company pursuant to chapter 5 of the Disclosure and Transparency Rules are given on page 142.

## Auditor

In accordance with the provisions of section 489 of the Companies Act 2006, a resolution for the appointment of PwC as auditor is to be proposed at the forthcoming Annual General Meeting. Each person who is a director at the date of approval of this Annual Report confirms that:

- so far as each director is aware, there is no relevant audit information of which the Company's auditor is unaware; and
- each director has taken all the steps that he or she ought to have taken as a director to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This statement is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

## Annual General Meeting

The 2019 Annual General Meeting will be held on 24 May 2019 in accordance with the notice being sent to shareholders with this report.

By order of the Board:

### U.S. Ball

Group Company Secretary  
8 March 2019

Springwood Court  
Springwood Close  
Tytherington Business Park  
Macclesfield  
Cheshire  
SK10 2XF

# Report of the Nomination Committee

Committee membership	No. of meetings 2018: 2	Main committee responsibilities
<b>Director</b>	<b>Attendance</b>	<ul style="list-style-type: none"> <li>Regularly review the structure, size and composition (including the skills, knowledge, experience and diversity) of the Board and make recommendations to the Board with regard to any changes.</li> <li>Give full consideration to succession planning for directors and other senior executives in the course of its work.</li> <li>Be responsible for identifying and nominating for the approval of the Board, candidates to fill Board vacancies as and when they arise.</li> </ul>
A.C. Quinn	2	
I.B. Duncan	2	
E. Lindqvist	2	
P. Larmon	2	
L. Chahbazi	2	

Dear Shareholders

I am pleased to introduce the Nomination Committee report for 2018. The Committee's key objective is to support the Board in fulfilling its responsibilities to ensure there is a formal, rigorous and transparent process for the appointment of new directors to the Board and to ensure that effective succession planning processes are in place across the Group.

The year commenced with the appointment of a new Non-Executive Director on 1 January 2018, Lili Chahbazi, at the same time as I started as Chair. The Committee will continue to focus on ensuring that the present and future composition of the Board is appropriate for the delivery of the Group's strategy and that all relevant UK Corporate Governance Code requirements continue to be met.

## A.C. Quinn

Chair of the Nomination Committee

## Role of the Nomination Committee

The Nomination Committee is a subcommittee of the Board, whose principal purpose is to advise on the appointment and, if necessary, dismissal of executive and Non-Executive directors. The Committee's terms of reference, which are listed on the Group's website, include all matters required by the UK Corporate Governance Code ('the Code'). Further information on the Code can be found on the Financial Reporting Council's website [www.frc.org.uk](http://www.frc.org.uk). The terms of reference are reviewed annually by the Group Company Secretary and the Chair, and any changes are then referred to the Board for approval. No changes were made to the terms of reference during the year.

## Key Activities

### Board composition/succession planning

- Supervised Board induction training
- Reviewed and updated succession plans for the Board and senior management

### Non-Executive directors

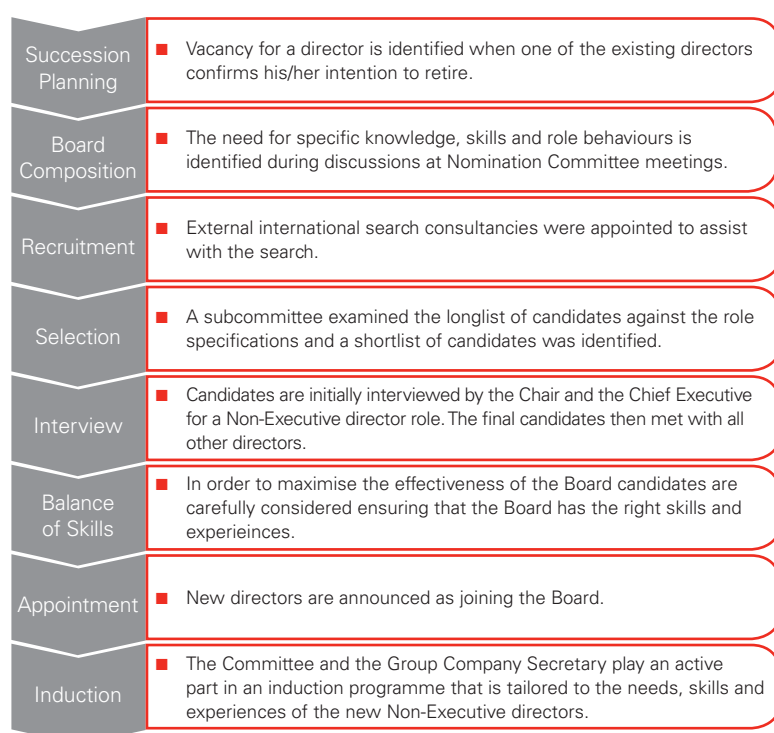
- Reviewed continued independence of the Non-Executive directors
- Reviewed the Non-Executive director time commitments and overboarding

### Diversity

- Reviewed the Group's diversity policy

### Governance and evaluation

- Reviewed the Committee's Terms of Reference
- Evaluation of Committee's effectiveness



## Composition of the Nomination Committee

As recommended by the Code, the Chair of the Board acts as the Chair of the Committee whose members also comprise the directors listed above. The Chair cannot chair the Committee when it is dealing with either the succession to the Chairship of the Group or the review of his or her own performance. Only members of the Committee have the right to attend the Committee meetings. Other individuals and external advisers may be invited to attend for all or part of any meeting when it is appropriate. The quorum necessary for the transaction of business is two.

The Group Company Secretary is secretary to the Committee.

The Committee has the authority to seek any information that is required, from any officer or employee of the Company or its subsidiaries. In connection with its duties, the Committee is authorised by the Board to take such independent advice (including legal or other professional advice, at the Group's expense) as it considers necessary, including requests for information from, or commissioning investigations by, external advisers.

## Director appointment policy and progress

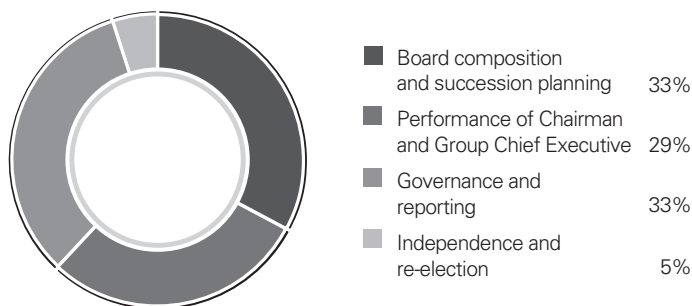
The Committee has developed a formal rigorous and transparent procedure for the appointment of new directors. Prior to making any appointment, the Committee, having evaluated the skills, experience and diversity of the Board, will determine the qualities and experience they seek and will then prepare a detailed description of the role with a view to appointing the most appropriate candidate. The Committee will use open advertising or the services of independent external advisers to facilitate the search.

A longlist of candidates will be drawn up, from which an appropriate number will be selected for interview. Upon completion the Committee will recommend to the Board the appointment of the preferred candidate.

## Board succession planning

A.C. Quinn commenced as Chair as of 1 January 2018 and Lili Chahbazi also joined the Board as a Non-Executive Director on 1 January 2018. There were no further changes to the Board structure during the year.

## Nomination Committee – allocation of agenda time



## Main activities of the Nomination Committee

In 2018 the Committee formally met two times and reviewed the composition and skills of the Board, with a view to considering the current and future skills and experience that the Board might require.

The Committee discussed succession planning and Board diversity, and reviewed the performance of the Group Chief Executive and other senior executives. In particular, the need to broaden the Board membership with respect to gender, ethnicity and age was discussed. The Committee has sought to ensure that appointments are of the best candidates to promote the success of the Company and are based on merit, with due regard for the benefits of diversity on the Board. Further information concerning Board diversity can be found on page 43 as part of the corporate governance statement. We are pleased to report that as of 1 January 2018 the female representation on the Board has been 43% compared to 17% in 2017.

The Committee considered and authorised the potential conflicts of interest which might arise where a director has fiduciary responsibilities in respect of other organisations. The Committee concluded that no inappropriate conflicts of interest exist. The Committee also assigned the Chair to review and agree with the Group Chief Executive his personal objectives for the forthcoming year.

Following the external Board evaluation in 2015, the Board agreed to undertake its next external evaluation during 2018. Further details of the review can be found in the Corporate Governance section of the Annual Report. Recommendations arising from the 2018 Board evaluation are in the process of being addressed.

In December 2018 the Nomination Committee reviewed the Board's size and composition, the frequency of the process for Board and Committee meetings, and best practice for dealing with Board issues including drawing up a training and/or induction programme for the directors. The terms of reference of the Committee were reviewed in conjunction with the Model Terms of Reference issued by the Institute of Chartered Secretaries and Administrators. The biographical details of the current directors can be found on pages 38 and 39. The Committee, having reviewed their independence and contribution to Board matters, confirms that the performance of each of the directors standing for re-election at this year's AGM continues to be effective and demonstrates commitment to their roles, including independence of judgement and time commitment for Board and Committee meetings. Accordingly the Committee has recommended to the Board that all current directors of the Company be proposed for re-election at the forthcoming AGM.

As Chair of the Committee, I will be available at the AGM in May 2019 to answer questions relating to the work of the Committee.

On behalf of the Nomination Committee:

### A.C. Quinn CBE

Chair of the Nomination Committee  
8 March 2019

# Report of the Audit Committee

Committee membership	No. of meetings 2018: 6	Main committee responsibilities
<b>Director</b>	<b>Attendance</b>	
I.B. Duncan	6	<ul style="list-style-type: none"> <li>■ Encourage and safeguard the highest standards of integrity, financial reporting, financial risk management and internal controls.</li> <li>■ Monitor the integrity of the financial statements including annual and half-yearly reports, trading updates and any other formal announcements relating to its financial performance. Review and report to the Board on significant financial reporting issues and judgements.</li> <li>■ Review the content of the Annual Report and advise the Board whether, taken as a whole, it is fair, balanced and understandable and provides the information necessary for shareholders to assess the Company's position and performance, business model and strategy.</li> <li>■ Monitor and review the adequacy and effectiveness of the Company's internal financial control and risk management systems including the robust assessment of principal risks.</li> <li>■ Oversee the relationship with the external auditor including consideration of fees, audit scope, terms of engagement, setting policy for the provision of non-audit services to make recommendations to the Board, subject to the approval by shareholders, on the appointment, reappointment or removal of the external auditor.</li> <li>■ Monitor and review the effectiveness of the Company's internal audit function.</li> <li>■ Review the adequacy and security of the Company's arrangements for its employees to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters.</li> </ul>
E. Lindqvist	6	
P. Larmon	6	
L. Chahbazi (appointed 1 January 2018)	6	

## Introduction & Objective

The Committee continues to focus on the integrity of Bodycote's financial reporting, risk management and internal controls and on the quality of the external and internal audit processes. The Committee will continue to keep its activities under review as the regulatory environment changes. Its objective is to provide effective governance over the Group's reporting, including the adequacy of related disclosures, the management and oversight of the Group's systems of internal control, financial risks and the performance of internal audit as well as the appointment and evaluation of the external auditor.

## Committee Membership & Meetings

The members of the Audit Committee are all independent Non-Executive directors. Their biographical details are shown on pages 38 to 39 and their remuneration on page 61. The Group Company Secretary is the secretary to the Audit Committee.

I.B. Duncan is Chairman of the Audit Committee. As a Chartered Accountant with strong experience in senior finance roles including Chairman of several other listed company audit committees. The Board considers that I.B. Duncan has recent and relevant financial, accounting and sector experience required to Chair the Committee.

All members of the Committee have significant and widespread experience in both executive and non-executive capacities of multinational industrial companies and are considered to have competencies relevant to their duties.

The Audit Committee met six times during 2018 and in March 2019: all members attended all meetings. The Committee Chairman also invited the Board Chair, Group Chief Executive, Chief Financial Officer, Group Financial Controller and Group Head of Risk (who is responsible for internal audit) to attend all regular meetings. Other executives from the Group were also invited, as appropriate, to attend meetings to provide a deeper level of insight into key issues. The Committee Chairman also invited the external auditor, Deloitte LLP ('Deloitte'), to every meeting with the exception of one meeting relating to the appointment of the new auditor. As part of the process of working with the Board to carry out its responsibilities and to maximise effectiveness, meetings of the Committee generally take place just prior to Board meetings.

I.B. Duncan also held preparatory meetings separately with Deloitte, the Group CFO, the Group Financial Controller and the Group Head of Risk prior to Committee meetings to review their reports and discuss issues in detail. Deloitte, the Group Head of Risk and the internal auditors (Ernst & Young LLP) met with the Audit Committee without the executives present.

## Main activities of the Committee during the year

The Committee is responsible for reviewing the half year results and the Annual Report and Accounts before recommending them to the Board for approval.

At its meetings, the Committee focused on the following main areas:

### Financial reporting

The primary recurring role of the Committee in relation to financial reporting has been to review, with management and the external auditor, the appropriateness and integrity of the interim and Annual Report and Financial Statements concentrating on, amongst other matters:

- the quality and acceptability of accounting policies and practices including interpretation of reporting standards and the adoption of policies;
- the application and impact of significant judgements, accounting estimates and matters where there was significant discussion with the external auditor;
- the clarity of disclosures and compliance with Financial Reporting Standards;
- the key points of disclosure and presentation to ensure the adequacy, clarity and completeness in the Annual Report and Financial Statements;
- whether the Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's strategy, business model and performance;
- reviewing with both management and Deloitte to ensure audit scoping was appropriate and that Deloitte had applied the necessary level of professional scepticism in performing their work; and
- reviewing various materials to support the statements on risk management and internal control and related disclosures made in the Annual Report and Financial Statements on this matter.

Reports from management were reviewed on significant matters, including litigation, accounting, treasury and tax matters and also reports from the external auditor on the outcome of their work.

The Committee reviewed and examined the half year and Annual Report and Financial Statements. Taken as a whole, in the light of their knowledge of the Group and its performance, the outcome of the activities described above and based on robust discussion with both management and the external auditor, the Committee has concluded that it is fair, balanced, consistent and understandable and provides the information necessary for shareholders to assess the Group's strategy, business model, position and performance, and reported to the Board accordingly.

During the year, the Group corresponded with the Financial Reporting Council (FRC) in respect of certain 2017 Annual Report disclosures. The comments received have been appropriately addressed and the FRC has closed all of its enquiries.

In addition to these matters, the Committee considered the following significant issues impacting the financial statements:

### Areas of focus

The areas of focus considered by the Committee in relation to the 2018 Annual Report included the following:

- *Leases.* The Committee reviewed progress toward the adoption of IFRS 16 'Leases'. The Committee oversaw the implementation of a new control process designed to ensure that Leases are accounted for and disclosed properly in the financial statements.
- *Impairment of assets.* The Committee reviewed and challenged the future forecast underlying the value in use calculation, and the assumptions, particularly the discount rate and growth factors, used in the discounted cash flow calculations for each cash generating unit, the sensitivity analysis applied and the projected future cash flows used to support the carrying values of the assets. Details of sensitivity analysis applied to key assumptions used in the impairment review as well as conclusions are set out in note 9 to the Financial Statements on page 109.
- *Restructuring, reorganisation and environmental provisions.* The Committee received reports, including from professional advisers, and challenged the basis and completeness of the assumptions used to calculate the provisions and the appropriateness of disclosures in the Report. The Committee discussed with management the key judgements behind provisions, taking note of the range of possible outcomes, and agreed with their recommendations.
- *Going concern and viability statement.* The Committee challenged the validity of the going concern assumption and viability statement used in the preparation of the Annual Report, in particular considering the Group's forecast for profits and cash generation, its liquidity position, available borrowing facilities and covenant compliance. Sensitivity analysis was undertaken to understand the impact of changes to key variables. The Committee also examined potential impacts that the UK Brexit may have on the above considerations and concluded that no material impact is expected.

The following are considered as key sources of estimation uncertainty in the financial statement notes:

- *Taxation.* A number of judgements are involved in calculating tax provisions and the level of deferred tax assets to be recognised. The Committee has focused on understanding and challenging the Group's critical tax risks and management's assessment and valuation of these risks. The Committee has supported enhanced transparency over the Group's tax risks and strategy in external reporting. Key risks, notably in the European Commission's State Aid enquiry, UK Brexit implications and internal cross border funding arrangements, have been reviewed and challenged including management's forecast of the future taxable profits of the relevant businesses.
- *Retirement benefits schemes.* Management took external professional advice in determining pension liabilities. The Committee reviewed and agreed the methods, assumptions used, and benchmarks, particularly in respect of inflation, the discount rate, life expectancy and the application of IFRIC 14 to the UK pension scheme, considering current norms and the sensitivity of the reported liability to changes in the assumptions. The Committee agreed the treatment and the corresponding disclosures on these matters. See note 29 of the financial statements.

### External audit

The Committee is responsible for managing the relationship with the Group's external auditor on behalf of the Board.

# Report of the Audit Committee continued

The Committee reviews and makes recommendations with regard to the reappointment of the external auditor each year. In making these recommendations the Committee considers auditor effectiveness and independence, partner rotation and any other factors which may impact the external auditor's reappointment. Deloitte has been the Group's external auditor for 17 years.

The external auditor is required to change the lead partner every five years and other partners periodically in order to protect independence and objectivity and provide fresh challenge to the Group. Mr M. Mullins has been lead partner since 2015.

At the May and October meetings Deloitte presented their audit plans for the interim review and year-end audit respectively. The Committee considered and challenged both the scope and materiality to be applied to the Group audit and its components. The Committee considered carefully the scope in respect of smaller and more remote locations and noted that the majority of local audits are undertaken by Deloitte.

During the year, the Committee initiated a tender process to change the Group's external auditor from 2019. See below for more information on the tender process.

## Assessment of Effectiveness

The Committee has adopted a formal framework for the review of the effectiveness of the external audit process and audit quality which includes the following aspects:

- assessment of the engagement partner, other partners and the audit team;
- audit approach and scope, including identification of risk areas;
- execution of the audit;
- interaction with management;
- communication with and support to the Audit Committee;
- insights, management letter points, added value and reports; and
- independence, objectivity and scepticism.

An assessment questionnaire was completed by each member of the Committee, the Chief Financial Officer and other senior finance executives. The feedback from the process is considered by the Audit Committee and provided to the external auditor and management. The full formal questionnaire is completed every three years with key areas being completed every year.

The Committee assessed the effectiveness of management in the external audit process by considering timely identification and resolution of areas of accounting judgement, the quality and timeliness of papers analysing those judgements and other documents provided for review by the external auditor and the Committee.

The Committee considered the FRC Audit Quality Review Team report on Deloitte LLP dated June 2018. If the audit is selected for quality review, the Committee understands that any resulting reports will be sent to the Committee by the FRC. After considering the above matters, the Committee felt that the external audit had been effective.

## Appointment of New Auditor

During the year, the Committee initiated a tender process to change the Group's external auditor from 2019. The tender was designed to be transparent, effective and efficient and give each participating firm an equal opportunity to successfully tender.

The tender process was supervised by the Committee, who made a formal recommendation to the Board on the external auditor appointment. To support them in this process, a Tender Panel was identified which included senior members of the Group's management and finance team.

The following process was followed:

- Five audit firms were invited to tender for the audit and related services and submit a final proposal document.
- Assurance was sought that each firm would be capable of being independent in the time frame required by applicable law or regulation before being appointed auditor. Due diligence activities conducted as part of the tender included a review of this independence.
- Following evaluation of resources, expertise, quality control and audit approach to deliver a high quality audit service to the Group, two audit firms submitted written proposals and gave oral presentations to senior members of the management and finance team which were evaluated.
- Objective criteria were established to ensure thorough and consistent process was followed when assessing the tender proposals. The criteria were weighted to take account of the relative importance to the overall outcome and included understanding of Bodycote's business, markets, operations and geographic scope. A broad range of factors were identified under each criterion to assist with the assessment process. These included approach to ensuring overall audit quality, experience and fit with Bodycote (the lead partner, team and the firm), the firm's international coverage and its alignment to Bodycote, the approach to managing the audit and working with other assurance providers, the value provided from the audit, the approach to transition, the approach to innovation and technology, and the performance of each firm during the proposal process. All the internal stakeholders involved were invited to rank/score each tender against each of these criteria to assist in the evaluation process.
- Both audit firms also provided Committee members with their written proposals and made oral presentations for the Committee to appraise. The Committee evaluated these proposals and presentations and considered both to be acceptable having both demonstrated they have the technical capabilities and people to deliver a high quality audit. This was subsequently presented to the Board. Further discussion between Committee members indicated an aligned preference to PwC as best suited and able to most easily effect the audit transition with the least disruption and impact on our business.



The Committee endorsed sharing its recommendation with the Board, together with the recommendation that a resolution be put to shareholders at the next AGM, proposing the appointment of PwC as Bodycote's external auditor from 2019.

Having undertaken this tender process in 2018 (in respect of the 2019 audit), PwC's appointment as Bodycote's external auditor meets the relevant requirements and recommendations relating to the tenure of appointment set out in The Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitive Tender Processes and Audit Committee Responsibilities) Order 2014 (the 'Order'), Regulation (EU) No. 537/2014 and the FRC's revised Ethical Standard June 2016. The Group complies with the provisions of the 'Statutory Audit Services for Large Companies Market Investigation Order 2014'.

### Non-audit services

The external auditor may be invited to provide services where their position as auditor renders them best placed to undertake the work. Financial due diligence, taxation, internal audit, and actuarial services are not typically contracted to the external auditor. No contracts in excess of £20,000 can be awarded to the external auditor without prior approval from the Committee Chairman or, in his absence, another member of the Committee. Non-audit fees paid to the auditor are shown in note 3 on page 105 and amounted to 11% (2017: 12%) of the audit fee.

### Independence

The independence of the external auditor has been confirmed by Deloitte every half year and was last confirmed in March 2019. The Committee considered Deloitte's presentation and confirmed that it considered the auditor to be independent.

### Internal audit

The internal audit plan for 2018 was presented to the Committee in October 2017. The plan takes account of the Group's strategic objectives and risks and provides the degree of coverage deemed appropriate by the Committee. The Committee reviewed and accepted the plan following discussions and challenge as to the scope and areas of focus. At each regular meeting the Group Head of Risk presented a report to the Committee on the status of internal audit plan, points arising from audits completed and follow up action plans to address areas of weakness. The status of these actions is monitored closely by the Committee until they are completed. The Committee also received reports on actual or suspected frauds and thefts by third parties and employees. None had any material financial impact on the Group and, where necessary, systems and procedures were altered to minimise the risk of recurrence.

The Group Head of Risk provides independent assurance over the key financial processes and controls in operation across the Group. The Group has engaged Ernst & Young LLP ('EY') to provide certain internal audit services.

Additional assurance has been obtained through a control self-assessment. Internal auditors have received self-certification from every plant and shared service centre that internal controls have been complied with and noting any non-compliance. A summary of results was presented to the Committee. The accuracy of returns is monitored by internal audit by verification visits to a random sample of sites.

The effectiveness of internal audit is reviewed and discussed annually with the Group Head of Risk and the EY engagement partner. An assessment questionnaire was completed by each member of the Committee, the Chief Financial Officer and other senior finance executives. The views of senior operational management have also been canvassed. The review takes into account the views of directors and senior management on matters such as independence, proficiency, resourcing and audit strategy, planning and methodology. On the appointment of a new engagement partner the Committee assesses the experience and expertise of the partner and other senior staff members. Audit quality is assured through a detailed review of each report being carried out by the Group Head of Risk, and a summary of each report's findings being reviewed by the Audit Committee. The review confirmed that the internal audit function was independent and objective and remained an effective element of the Group's corporate governance framework.

### Risk management

The Committee monitored the effectiveness of the Group's risk management and internal control systems through updates at each meeting from the Group Head of Risk who has responsibility for developing the Group's risk management and internal controls framework.

The Committee reviewed changes to the principal risks and mitigating actions identified by management. The Committee also received regular reports on issues raised via the Open Door Line (an external independent service where employees may report matters of concern) and assessed both how such calls are dealt with and whether there was any indication of material risk. During 2018 there were 18 Open Door cases, all of which were investigated and closed during the year, with appropriate action taken where necessary.

### Internal control

At each meeting the Committee considered and challenged reports from the internal auditors on the effectiveness of internal controls. The Committee also performed an annual review of the Group's internal control processes and considers the system to be effective and in accordance with the Guidance on Risk Management, Internal Control and Related Financial and Business Reporting as issued by the FRC (September 2014).

### Committee evaluation

The Committee's activities formed part of an internal review of Board effectiveness which was undertaken in September and October 2018 and approved by the Board in December 2018. There were no material deficiencies noted in the review and directors indicated a high level of satisfaction with the work of the Committee. Based on this, and as a result of the work done during the year, the Committee has concluded that it has acted in accordance with its terms of reference and carried out its responsibilities effectively.

On behalf of the Audit Committee:

#### I.B. Duncan

Chairman of the Audit Committee  
8 March 2019

# Board report on remuneration

Committee membership	No. of meetings 2018: 6	Main committee responsibilities
<b>Director</b>	<b>Attendance</b>	
E. Lindqvist	6	<ul style="list-style-type: none"> <li>■ Responsibility for setting the remuneration policy for all executive directors and the Company's Chair.</li> <li>■ Recommend and monitor the level and structure of remuneration for senior management.</li> <li>■ Review the ongoing appropriateness and relevance of the remuneration policy.</li> <li>■ Appoint remuneration consultants.</li> <li>■ Approve the design of and determine targets for executive directors' and other senior executives' performance-related pay schemes.</li> <li>■ Review the design of all share incentive plans for approval by the Board and shareholders. Determine whether awards will be made on an annual basis.</li> </ul> <p><i>These responsibilities are currently under review based on the contents of the revised Corporate Governance Code.</i></p>
I.B. Duncan	6	
P. Larmon	6	
L. Chahbazi	6	

## Chair's letter

As Chair of the Remuneration Committee ('the Committee') and on behalf of the Board of Directors, I am pleased to present our Board report on remuneration for the 2018 financial year, in line with the requirements of the Large and Medium sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013.

## Structure of report

This year, in accordance with regulatory requirements, we will bring a new policy to shareholders at the 2019 AGM, at which point our previous policy (as approved at the 2016 AGM), expires. Our report is therefore structured as follows:

- **Section A:** This describes how the existing policy, approved at the 2016 AGM, was applied in 2018;
- **Section B:** This sets out our proposed remuneration policy. It is also available on our website at [www.bodycote.com/en/investors/reports-and-results/2018.aspx](http://www.bodycote.com/en/investors/reports-and-results/2018.aspx)

## The UK Corporate Governance Code

The revised UK Corporate Governance Code represents some of the most significant changes to the work of the Committee to occur in recent years. The Committee fully endorses the requirements and underlying intent of the Code and we will continue to ensure we operate in compliance with its requirements. Focusing on simplicity and strategic alignment is fundamental to our thinking, alongside a desire to create long-term alignment between management and the shareholder experience. We also recognise the importance of considering wider stakeholders – including our employees – in our decision making processes. The Committee is working together with the Company's human resources team to ensure the Committee can best support the Board in its new overarching responsibility to ensure workforce policies and practices are in line with culture and strategy, and will report on our approach in due course.

In developing the revised Policy we considered the Principles prescribed by the revised Code around Clarity, Simplicity, Risk, Predictability, Proportionality and Alignment to culture. We believe that our new policy fully and appropriately addresses each of these areas.

## Business performance and incentive outcomes for 2018

Bodycote has performed strongly through 2018, with Group revenue growth of 5.6% after a negative impact from foreign exchange of 1.4%. Across all our core markets, revenues have grown significantly, with 8% growth in civil aviation. Through a targeted programme of investments in Emerging Markets we have delivered revenue of 21%, and our Specialist Technologies business grew revenues at 12%. Group return on sales also increased 1 percentage point to 19.0%. We believe that the incentive payouts we have made to our executive directors reflects this performance and is aligned to the overall performance of the Company. As such, the Committee determined that no discretionary adjustments (either upward or downward) would be required from the formulaic outcomes.

### Annual bonus

We have faced challenging cost inflation headwinds, but through price increases and a continued focus on cost discipline and operational efficiencies we have been able to recover the majority of the impact this has had. The Group's headline operating profit grew 12% to £138.3m. Our headline operating cash flow has also grown by 15% to £128.7m, supporting our ability to return cash to our shareholders. As these measures are our core internal financial metrics they form the core annual bonus metrics. The annual bonus also contains a personal element (weighted to 13% of the total) that primarily reflects how our executive directors have delivered on our strategic goals, and in particular our investments in growth. Given the strength of our strategic implementation and the extent to which this has been reflected in financial performance, the outcome under the personal measure of 80% for the CEO and 70% for the CFO are appropriate in the context of the overall performance of the Business.

The annual bonus therefore paid out at 68.5% of maximum for the CEO and 67.2% of maximum for the CFO, of which 35% will be deferred into shares for three years, in line with our approved policy for bonus deferral.

### Long-term incentive

The Company's principal long-term incentive, the Bodycote Incentive Plan (BIP) is based on performance against return on capital employed (ROCE) and earnings per share (EPS) targets over a three year period. Our ongoing focus on operating efficiency, margins, and targeted investments in high growth markets has supported earnings development over the three year period despite the challenging environment, resulting in an outcome of 100% under this measure. Strong returns have also been delivered, helped by the focus on capital investment in specialist markets, and ROCE performance was 78.5% of maximum.

The 2015 Co-Investment Plan (CIP) is based on absolute total shareholder returns growth, and the TSR CAGR value of 34.1% we have delivered over the three year performance period is reflected in a final vesting under this plan of 98.4%. This plan no longer forms part of our active policy and this represents the final vesting under the CIP.

### Revised remuneration policy

Through the course of the year the Committee has considered carefully our strategic objectives and how our incentive structure (as approved at the 2016 AGM) supports this. We also recognise the commentary in the Code that relates to incentive arrangements, and the views of investors and proxy bodies on different models of pay and package structure. We firmly believe that our current structure continues to be fit for purpose, and we will therefore not be proposing any significant changes to our new policy (which we currently anticipate will run to AGM 2022). In addition, we believe that the structure in totality is well aligned to the purpose and values of the business.

We will however make a number of small amendments to ensure we are aligned with the relevant areas of best practice, including:

- Increasing our shareholding requirement for the CFO to 200% of salary.
- Incorporating a formal two year post-vest holding period for the BIP into our policy.
- In recognition of the views of shareholders and the revised Code, our pension provisions for new Executive Directors are being reduced. The company contribution will be set at the time of appointment to align to that of other employees as part of our ongoing process to align Executive Director's pension to those of the other employees legacy contributions (or cash equivalents) of up to and including 25% of salary remaining in place for current Executive Directors.
- We are further increasing the protection our clawback and malus policy provides through extension of our trigger clauses to include reputational damage.

In reviewing our policy we consulted extensively with our largest shareholders together with proxy agencies, and discussed the rationale for our proposals. We received an overwhelmingly positive response, recognising the success of our historic remuneration framework in driving exceptional business performance over the last three-year period and the alignment of our new proposals with investor expectations and corporate governance requirements.

We further consulted with shareholders concerning a one-off salary increase of 10% for our Chief Executive reflecting the increased complexity and significant growth of our Company in recent years, coupled with an excellent performance in his role. However, reflecting feedback received from shareholders, we have decided to amend our original decision and Stephen Harris will instead receive an inflationary increase of 3%, in line with the average increase of the wider UK workforce.

### Application of policy for 2019

We set out below a brief overview of our intended application of policy for 2019.

- **Base salaries:** The Committee is also proposing an increase of 3% for the CEO and the CFO in line with the general employee population.
- **Benefits and pension:** There will be no changes to benefits and pension provided to our executive directors.
- **Annual bonus:** The maximum bonus opportunity remains 200% of salary for the CEO and 150% of salary for the CFO, with 35% of any bonus paid being deferred in shares for three years. The measures and weightings used have been reviewed and we believe a bonus consisting of 77% headline operating profit, 10% headline operating cash management and 13% personal objectives continues to enable the annual bonus to be aligned to the Company's strategy and ensures our executives are focused on delivery of improved profitability and control on working capital.
- **Bodycote Incentive Plan (BIP):** Award levels will remain 175% of salary for Executive Directors. Similarly, measures and weightings have been reviewed and we believe the equal focus on returns and earnings is strongly aligned with our strategic priorities. The growth of our business and our ability to deliver strong and sustainable returns to investors is based on delivery of an effective deployment of capital in rapid growth areas and on acquisitions, which ROCE and EPS continue to create alignment to.

I trust the information presented in this report enables our shareholders to understand both how we have operated our remuneration policy over the year and the rationale for our decision making. We remain fully committed to continuing an open and transparent dialogue with our shareholders. I would welcome your views on our policy, the content of this report or any other items you would like to discuss and I look forward to meeting you and answering any questions you may have at the AGM.

#### E. Lindqvist

Chair of the Remuneration Committee  
8 March 2019

This report has been structured to support the reader in quickly and easily accessing relevant information.

Main body	Page
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Section A: Implementation of Policy	59
Section A: Annual Report on Remuneration	61
Section B: Remuneration Policy	68

1. Legacy contributions for cash equivalents of up to and including 25% of salary remain in place for current Executive Directors.

# Board report on remuneration continued

## Section A Remuneration at a glance

This introduction provides a high-level overview of the remuneration received by our Executive Directors. Full details can be found in the Annual Report on Remuneration.

### Single figure of remuneration for Executive Directors

Incumbent	Financial year	Total salary/fees (£000)	Total pension (£000)	Total other benefits (£000) <sup>1</sup>	Annual bonus (£000)	Total BIP <sup>2</sup> (£000)	Total CIP (£000)	Dividend equivalent for BIP + CIP (£000)	Total (£000)
S.C.Harris	2018	542	135	22	742	1,040 <sup>2</sup>	50	118	<b>2,649</b>
	2017	527	132	27	1,031	500 <sup>3</sup>	34	44	<b>2,295</b>
D.Yates	2018	391	98	17	394	–	–	–	<b>900</b>
	2017	380	95	26	548	–	–	–	<b>1,049</b>

- Other benefits consist of company car (or allowance), family level private medical insurance, salary supplement in lieu of pension life assurance cover and sick pay. Certain other expenses incurred in pursuit of bona fide business activities are, under UK tax regulations, treated as a taxable benefit in kind, and the director has received grossed up compensation for this in order to leave him in a neutral position.
- An estimated market price at vesting was used and this was calculated as the three months average from 1 October to 31 December 2018 of £768.
- An estimated share price of £9.11 at close of markets on 5 March 2018 was used to estimate the value in the 2017 Annual Report. This has now been updated with the share price of £9.33 at the close of markets on the vesting date of 12 March 2018.

### Annual performance related bonus

The 2018 annual bonus was based on three elements – headline operating profit, headline cash management and personal objectives. Stretching targets were set in the context of the challenging market conditions we faced and the investments that were planned in the year. Following strong performance in the year the bonus paid out at 68.5% for the CEO and 67.2% for the CFO, 35% of the award will be deferred in shares for both the CEO and the CFO. The performance targets and actual performance are set out below. Targets are set on a constant currency basis so as to remove the positive and negative impact of currency fluctuations from the annual bonus.

	% of award	Threshold	Target	Maximum	Actual performance achieved	Outcome			
						S.C. Harris		D. Yates	
						% of max	% of salary	% of max	% of salary
Group headline operating profit	77%	£124.5m	£139.3m	£146.3m	£138.3m	77%	96%	77%	72%
Group headline operating cash flow	10%	£104.4m	£116.0m	£116.0m	£128.7m	100%	20%	100%	15%
Personal scorecard	13%					80%	21%	70%	14%
					<b>Total</b>	<b>69%</b>	<b>137%</b>	<b>67%</b>	<b>101%</b>

### Bodycote Incentive Plan (BIP)

BIP awards made in 2016 had a three-year performance period ending on 31 December 2018, with 50% of the award subject to satisfaction of a ROCE target and 50% subject to the headline earnings per share (EPS) target. Over this period our total shareholder returns have increased by 34%, demonstrating the returns we have made to shareholders. This is reflected in the 89.3% of max vesting of the BIP. The threshold and maximum targets along with the vesting schedule are set out in the tables below.

	ROCE		Headline EPS	
	Performance target	Vesting of element (% of maximum)	Performance target	Vesting of element (% of maximum)
Threshold performance	15.5%	0%	31.7p	0%
Maximum performance	23.0%	100%	52.0p	100%
Performance achieved	20.5%	39.3%	55.9p	50%

### 2016 BIP outcome

S.C. Harris	89.3% of maximum opportunity
D. Yates	n/a
D Landless (retired 31 Dec 16)	The 2016 BIP award lapsed on D Landless's leaving date

### Legacy Co-Investment Plan (CIP)

Until 2015 Executive Directors were invited annually to purchase shares up to 40% of basic salary (net of tax) against which performance based matching shares are granted on a 1:1 basis. CIP awards are subject to an absolute TSR target. No further awards will be made under this plan and the 2015 CIP that vested in 2018 was the final such award. The CIP awards made in 2015 had a three-year performance period ending on 30 April 2018.

The absolute TSR performance targets applicable to this award are set out below.

Absolute TSR performance target	Vesting level
4% CAGR + CPI	50% (0.5:1 match)
10% CAGR + CPI	100% (1:1 match)

Over the three-year period, the Group achieved absolute annual TSR growth of 11.6%, reflecting the value we have delivered to our shareholders over this period. This performance resulted in a vesting of 98.4% under the plan. The number and value of shares which vested for S.C. Harris is set out on page 63. As D.F. Landless is no longer an Executive Director, vesting under this plan to him is set out under payments to past directors.

### Shareholding requirements

Executive directors and other senior executives are expected, within five years of appointment, to build up a shareholding in the Company. For the purposes of this requirement, only beneficially owned shares and the value of deferred shares under the annual bonus will be counted. The table below sets out the minimum shareholding requirements, as a percentage of salary, for the Chief Executive and for the Chief Financial Officer, noting that both holding requirements have been reached.

Shareholding requirements	Minimum shareholding requirement	Current shareholding <sup>1</sup>
S.C. Harris	200%	291%
D. Yates	200%	372%

1. At the 31 December 2018 share price.

### Implementation of the Remuneration Policy in 2019

The table below provides information on how our Remuneration Policy will be implemented in 2019.

Element of pay	Implementation for 2019																											
<b>Total salary</b>	<p>Base salaries are reviewed on an annual basis.</p> <p>S.C. Harris will receive a salary of £558,181 in 2019, an increase of 3% (2018: £541,923).</p> <p>D. Yates will receive a salary of £402,751 in 2019, an increase of 3% (2018: £391,020).</p> <p>Note that Non-Executive Director fees will next be reviewed at the March 2019 meeting of the Committee, and the outcome of this review will be disclosed in the following year's report.</p>																											
<b>Pension and benefits</b>	<p>No changes proposed.</p> <p>Executive Directors receive a salary supplement in lieu of pension at a rate of 25% of base salary.</p>																											
<b>Annual bonus</b>	<p>No change to maximum opportunity: 200% of base salary for CEO, 150% of base salary for CFO.</p> <p>The performance measures and their relative weightings also remain unchanged: 77% operating profit, 10% operating cash management and 13% personal objectives.</p> <p>The Committee reviews the performance measures and targets on an annual basis to ensure that they remain appropriately aligned to the overall business strategy but do not encourage excessive risk taking.</p> <p>The Committee has determined that performance targets will not be disclosed on a prospective basis for reasons of commercial sensitivity, but will be disclosed on a retrospective basis in next year's Annual Report on Remuneration to the extent that the Committee determines that the measures are no longer commercially sensitive.</p>																											
<b>Bodycote Incentive Plan (BIP)</b>	<p>No change to maximum opportunity: 175% of base salary for Executive Directors.</p> <p>The performance measures and their relative weightings also remain unchanged: 50% ROCE and 50% headline EPS.</p> <p>The targets for the 2019 BIP awards are disclosed below and ensure that the Committee are able to deliver upper quartile reward for upper quartile performance. ROCE targets currently do not reflect the impact anticipated from IFRS 16 (leases) and the Committee is currently still to determine whether this should be reflected in these targets.</p> <table border="1" style="width: 100%; margin-top: 10px;"> <thead> <tr> <th colspan="3">BIP targets for 2019 award</th> </tr> <tr> <th>Performance metric</th> <th>Headline EPS</th> <th>ROCE*</th> </tr> </thead> <tbody> <tr> <td>Weighting (% of total award)</td> <td>50%</td> <td>50%</td> </tr> <tr> <td>Performance period</td> <td>3 years</td> <td>3 years</td> </tr> <tr> <td>Threshold performance</td> <td>56p</td> <td>15%</td> </tr> <tr> <td>Vesting level</td> <td>0%</td> <td>0%</td> </tr> <tr> <td>Maximum performance</td> <td>64p</td> <td>23%</td> </tr> <tr> <td>Vesting level</td> <td>Full vesting</td> <td>Full vesting</td> </tr> <tr> <td>EPS underpin</td> <td>47.6p</td> <td></td> </tr> </tbody> </table>	BIP targets for 2019 award			Performance metric	Headline EPS	ROCE*	Weighting (% of total award)	50%	50%	Performance period	3 years	3 years	Threshold performance	56p	15%	Vesting level	0%	0%	Maximum performance	64p	23%	Vesting level	Full vesting	Full vesting	EPS underpin	47.6p	
BIP targets for 2019 award																												
Performance metric	Headline EPS	ROCE*																										
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Maximum performance	64p	23%																										
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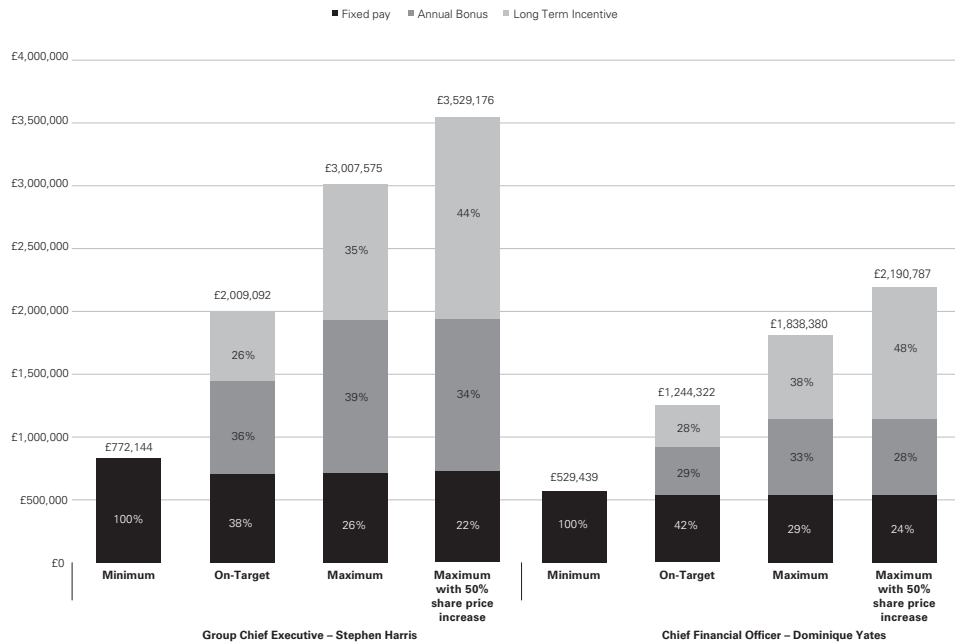
\* on a pre-IFRS 16 basis

During the year, the Committee reviewed the BIP structure and measures in the context of our strategic priorities over the coming three years. The Committee determined that the current framework continues to appropriately support delivery of our strategic plan.

# Board report on remuneration continued

## Illustration of application of remuneration policy for 2019

The remuneration package for the Executive Directors is designed to provide an appropriate balance between fixed and variable performance-related components. The Committee is satisfied that the composition and structure of the remuneration package is appropriate, clearly supports the Company's strategic ambitions and does not incentivise inappropriate risk taking. This is reviewed on an annual basis. The chart below sets out illustrations of the impact of share price appreciation on the composition and value of each Executive Director's remuneration package, should they achieve minimum, at-target or maximum performance. This disclosure is in line with The Companies (Miscellaneous Reporting) Regulations 2018.



For the purposes of the above analysis, the following methodology has been used:

- Fixed elements comprise base salary and other benefits:
  - Base salary reflects the base salary as at 1 January 2019.
  - Benefits reflect benefits received in 2018 (including pension).
- For on-target performance, an assumption of 60% of annual bonus is applied and vesting of 50% of the maximum for the BIP.
- For the minimum, on-target and maximum basis bars no share price increase has been assumed or dividend reinvestment.
- Fixed elements are salary, benefits and pension.
- Annual variable element is the annual bonus both cash and deferred shares.
- Long-term variable element is the BIP award and dividend equivalents.

## Annual report on remuneration

This section provides details of remuneration outcomes for executive directors who served during the financial year ended 31 December 2018. This section of the report is audited and subject to an advisory vote by shareholders at the 2019 AGM.

### Auditable section

#### Total single figure table

Incumbent	Financial year	Total salary/fees (£000)	Total pension (£000)	Total other benefits <sup>1</sup> (£000)	Annual bonus (£000)	Total BIP (£000)	BIP value at grant price (£000)	Share price gain on vesting of BIP between grant and vest date	Total CIP <sup>4</sup> (£000)	Total (£000)
<b>Executive Directors</b>										
S.C. Harris	2018	542	135	22	742	1,154 <sup>2</sup>	782	259	54	<b>2,649</b>
	2017	527	132	27	1,031	541 <sup>3</sup>	408	89	37	<b>2,295</b>
D. Yates	2018	391	98	17	394	–	–	–	–	<b>900</b>
	2017	380	95	26	548	–	–	–	–	<b>1,049</b>
<b>Non-Executive Directors</b>										
A.C. Quinn <sup>6</sup>	2018	225	–	–	–	–	–	–	–	<b>225</b>
	2017	–	–	–	–	–	–	–	–	–
A.M. Thomson <sup>5</sup>	2018	–	–	–	–	–	–	–	–	–
	2017	200	–	1	–	–	–	–	–	<b>201</b>
P. Larmon	2018	56	–	2	–	–	–	–	–	<b>58</b>
	2017	54	–	6	–	–	–	–	–	<b>60</b>
E. Lindqvist	2018	63	–	–	–	–	–	–	–	<b>63</b>
	2017	63	–	2	–	–	–	–	–	<b>65</b>
I.B. Duncan	2018	74	–	–	–	–	–	–	–	<b>74</b>
	2017	72	–	–	–	–	–	–	–	<b>72</b>
L. Chahbazi <sup>7</sup>	2018	56	–	–	–	–	–	–	–	<b>56</b>
	2017	–	–	–	–	–	–	–	–	–

#### Notes accompanying the total single figure table

- Other benefits consist of company car (or allowance), family level private medical insurance, life assurance cover and sick pay. Certain other expenses incurred in pursuit of bona fide business activities are, under UK tax regulations, treated as a taxable benefit in kind, and the directors have received grossed up compensation for this in order to leave him/her in a neutral position.
- The 2018 figures relate to BIP awards made in 2016 with performance periods ending on 31 December 2018. Shares vested as the targets were achieved at 156.2% out of 175% (equivalent to 89.3% of maximum opportunity). This includes dividend equivalents. For 2018 dividend equivalents for S.C. Harris were £114,063. An estimated market price at vesting was used of £7.68 calculated as the three-month average from 1 October to 31 December 2018.
- This included dividend equivalents. An estimated share price of £9.11 at close of markets on 5 March 2018 was used to estimate the value in the 2017 Annual Report. This has now been updated with the share price of £9.33 at the close of markets on the vesting date of 12 March 2018.
- The 2018 figures relate to CIP awards made in 2015 with performance periods ending 30 April 2018. The shares vested on 31 May 2018 at a share price of £9.93. This includes dividend equivalents. For 2018, dividend equivalents for S.C. Harris were £4,191.
- A. Thomson retired as Chairman and Non-Executive director on 31 December 2017.
- A.C. Quinn commenced as Chair on 1 January 2018.
- L. Chahbazi commenced as Non-Executive director on 1 January 2018.

The base salaries of the Executive Directors are reviewed in January every year. As described in Section B: Directors' Remuneration Policy, a number of factors are taken into account when salaries are reviewed, including companies of a similar size and complexity, and the individual's role, experience and performance, as well as a consideration of market level salaries payable in FTSE 250. The table below sets out the base salary figures for 2019 along with comparative figures for 2018.

Name	Position	Salary from 1 January 2018	Salary from 1 January 2019	Salary increase
S.C. Harris	Group Chief Executive	£541,923	£558,181	3%
D. Yates	Chief Financial Officer	£391,020	£402,751	3%

### Pension

S.C. Harris and D. Yates are entitled to a salary supplement in lieu of pension at a rate of 25% of basic salary. In addition, a death in service benefit of eight times basic salary is payable.

### Taxable benefits

The Group provides other cash benefits and benefits in kind to directors as well as sick pay and life insurance. These include the provision of company car (or allowance) and family level private medical insurance.

Name	Car/car allowance	Fuel	Healthcare	Other taxable benefits*
S.C. Harris	£17,560	£2,400	£1,711	–
D. Yates	£12,000	£1,200	–	£3,499

\* Certain other expenses incurred in pursuit of bona fide business activities are, under UK tax regulations, treated as a taxable benefit in kind, and the director has received grossed up compensation for this in order to leave him/her in a neutral position.

# Board report on remuneration continued

## Incentive outcomes for 2018

### Annual performance related bonus

The table below provides the details of the annual bonus awards received in respect of the Group and individual performances in the 2018 financial year.

The annual bonus potential for the period to 31 December 2018 for Executive Directors was split 77% in respect of Group headline operating profit, 10% on Group headline operating cash flow and 13% on personal strategic objectives. These performance conditions and their respective weightings reflected the Committee's belief that any incentive compensation should be linked both to the overall performance of the Group and to those areas of the business that the relevant individual can directly influence.

Stretching targets were set in the context of the challenging market conditions we faced and the investments that were planned in the year. Following strong performance in 2018, the bonus paid out at 68.5% for the CEO and 67.2% for the CFO, 35% of the award will be deferred in shares, for the both the CEO and the CFO. The performance targets and actual performance are set out below.

	% of award	Threshold	Target	Maximum	Actual performance achieved	Outcome			
						S.C. Harris		D. Yates	
						% of max	% of salary	% of max	% of salary
Group headline operating profit	77%	£124.5m	£139.3m	£146.3m	£138.3m	77%	96%	77%	72%
Group headline operating cash flow	10%	£104.4m	£116.0m	£116.0m	£128.7m	100%	20%	100%	15%
Personal scorecard	13%					80%	21%	70%	14%
					Total	69%	137%	67%	101%

### Personal Scorecard

**Executive Director** Stephen Harris

**Overview** For 2018 Stephen's objectives were: drive growth in emerging markets, drive increased growth in Specialist Technologies, drive sales strategy forward, ensure ERP system is reviewed, transition leadership of selected internal departments, provide SHE leadership and support internal processes

**Key achievements in the year**

- As reflected in performance under our core EPS measure, the Group delivered strong top line sales growth of 5.6% in 2018, which exceeded the outperformance target the Committee had agreed with the CEO.
- Specific focus areas for the CEO were the achievement of year on year growth in Specialist Technologies and emerging market revenues. In 2018 Specialist Technologies sales grew by 12% on 2017 and emerging markets grew by 21%, in both cases outperforming the objectives.
- The Board tasked the CEO with increasing the levels of sales. Achievement here was in line with the target set.
- The Group is reviewing its Enterprise Resource Planning (ERP) programme that will ensure our IT systems support the effective and efficient operation of our business into the future. Progress required in 2018 was met. Review to be completed in 2019.
- Succession planning is a key challenge for our business and is therefore central to the CEO's objectives. As such his personal objectives required him to transition the leadership of a number of key departments in the year, which was achieved. Actual achievement of succession planning in the year exceeded this, with the next level of management in these departments also refreshed.
- The personal objective was around the promotion and implementation of Safety, Health and Environmental processes. This metric is clearly a critical part of the CEO's role and the Committee determined that he had effectively fulfilled this objective in the year taking into account careful consideration of feedback from the Group SHE Committee.

**Rating** The Committee assessed achievement for all objectives with an overall rating of 80%

**Executive Director** Dominique Yates

**Overview** For 2018 Dominique's objectives were: define and implement Group IR strategy; recruitment of key finance personnel; review of the ERP system

**Key achievements in the year**

- The CFO was tasked with defining and implementing a new Group Investor Relations strategy in the year. This objective was achieved, and we believe that through this IR strategy the Group will maintain strong relationships and continue productive two-way dialogue with our shareholders.
- Succession planning features in the personal objectives for both our CEO and CFO, and as part of this the CFO was tasked with filling a number of key vacant finance roles across the business. All relevant roles were filled within the required time-frame and so this objective was achieved in full.
- The CFO shared an objective with the CEO around the review of the Enterprise Resource Planning (ERP) programme. Progress required in 2018 was met. Review to be completed in 2019.

**Rating** The Committee assessed achievement for all objectives with overall rating of 70%.



### Bodycote Incentive Plan (BIP)

BIP awards made in 2016 had a three-year performance period ending on 31 December 2018, after which they will vest immediately, with 50% of the award subject to satisfaction of a ROCE target and 50% subject to the headline earnings per share (EPS) target.

Over this period total shareholder returns of 21% were achieved demonstrating the strength of the returns we have made to shareholders. The threshold and maximum targets along with the vesting schedule are set out in the tables below.

	ROCE		Headline EPS	
	Performance target	Vesting of element (% of maximum)	Performance target	Vesting of element (% of maximum)
Threshold performance	15.5%	0%	31.7p	0%
Maximum performance	23.0%	100%	52.0p	100%
<b>Performance achieved</b>	<b>20.5%</b>	<b>78.5%</b>	<b>55.9p</b>	<b>100%</b>

If headline EPS at the end of the performance period was below 27p, then no awards will vest. Over the period, ROCE was 20.5% and the headline EPS figure for the year was 55.9p.

The table below sets out the 2016 BIP outcome for S.C. Harris. D.F. Landless 2016 BIP award lapsed on his retirement date of 31 December 2016.

#### 2016 BIP outcome

S.C. Harris	89.3% of maximum opportunity
-------------	------------------------------

The table below sets out a summary of shares vesting for BIP awards made in 2016 for S.C. Harris.

Executive	Award type	Grant date	Number of shares granted	End of performance period	% award vesting	Number of shares vesting	Vesting date
S.C. Harris	2016 BIP	13 April 2016	151,767	31 Dec 18	89.3%	135,467	11 Mar 19

### Legacy Co-Investment Plan (CIP)

As described in Section B: Directors' Remuneration Policy, CIP awards are subject to an absolute TSR target. Executive Directors were invited to purchase shares up to 40% of basic salary (net of tax) against which performance based matching shares are granted on a 1:1 basis. The CIP awards made in 2015 had a three-year performance period ending on 30 April 2018, and vested on 31 May 2018. The absolute TSR performance targets applicable to this award are set out below.

Absolute TSR performance target	Vesting level
4% CAGR + CPI	50% (0.5:1 match)
10% CAGR + CPI	100% (1:1 match)

Over the three-year period, the Group achieved absolute annual TSR growth of 11.6%. This strong return to shareholders over the period is reflected in the vesting of 98.4% under the CIP. Note that awards are no longer made under the CIP.

The number of shares which vested for S.C. Harris is set out below. As D.F. Landless is no longer an Executive Director, vesting under this plan to him is set out under payments to past directors.

### Scheme interests awarded in the financial year

#### CIP awards granted during the year

No awards were made under the CIP – the final award was made in 2015 with vesting occurring in May 2018. This plan no longer features in the Company's policy.

#### BIP awards granted during the year

Awards consisting of conditional shares were granted to both Executive Directors, equivalent in value to 175% of their base salaries on 18 May 2018, and will vest after three years in March 2021. The performance period will end on 31 December 2020. Details of the awards are set out below. Awards are subject to continued employment and the achievement of ROCE and headline EPS growth performance targets, as summarised in the table below.

The Committee has reviewed the performance targets and these have been revised appropriately to ensure that they remain stretching targets which underpin the Group's objectives. Our long-term targets reflect the continued challenges in the wider commercial environment and the improved growth we expect to see following our emphasis on operational efficiency and the expansion of our footprint in rapid growth territories.

	ROCE		Headline EPS	
	Performance target	Vesting of element (% of maximum)	Performance target	Vesting of element (% of maximum)
Threshold performance	17%	0%	50p	0%
Maximum performance	23%	100%	64p	100%

If headline EPS at the end of the performance period is below 42.5p, then no awards will vest. The Committee has decided that the ROCE figure of 23% is a robust aspiration for the Group in view of our expected programme of investments, recognising the potential for

# Board report on remuneration continued

unintended consequences in terms of short-term capital underinvestment for the business. Dividend equivalents are payable in respect of those shares that vest.

The number of shares that were awarded, at a grant price of £9.51, to the Executive Directors during the year is set out below.

Executive	Award type	Grant date	Number of shares	Market price at date of award	Face value at date of award
S.C. Harris	2018 BIP	12 April 2018	96,911	£9.51	£921,624
D. Yates	2018 BIP	12 April 2018	69,924	£9.51	£664,977

## Chair and Non-Executive Directors' fees

Fees were reviewed against comparable companies of similar size and were effective as of 1 January 2018. The fee payable to the Chair of the Board and other Non-Executive Directors were as follows:

Individual	Roles	Fee for 2018	Fee for 2017	% increase in NED role fees
Eva Lindqvist	■ Non-Executive Director	£65,182	£63,345	2.9%
	■ Chair of Remuneration Committee			
	■ Member of Audit, Remuneration and Nomination Committees			
Ian Duncan	■ Non-Executive Director	£74,415	£72,318	2.9%
	■ Chair of Audit Committee			
	■ Member of Audit, Remuneration and Nomination Committees			
	■ Senior Independent Director			
Patrick Larmon	■ Non-Executive Director	£55,549	£54,372	2.9%
	■ Chair of Employee Advisory Committee			
	■ Member of Audit, Remuneration and Nomination Committees			
Lili Chahbazi	■ Non-Executive Director	£55,549	–	–%
	■ Member of Audit, Remuneration and Nomination Committees			
Anne C. Quinn	■ Non-Executive Chair	£225,000	–	–%
	■ Chair of Nomination Committee			
	■ Member of Nomination Committee			

Non-Executive Director fees were increased for 2018 based on market benchmarking against Non-Executive Director fees in the FTSE 250 and other companies of similar size and complexity in line with the Policy approved at the 2016 AGM.

The fee for the new Chair, Anne C Quinn, was set at £225,000 to reflect her experience and the skills she will bring to the role. In determining the appropriate fee level the Committee considered market benchmarking against the FTSE 250 and other companies of comparable size and complexity in line with the policy approved at the 2016 AGM.

At 31 December 2018 the aggregate annual fee for all Non-Executive Directors, including the Chair, was £475,695, which is below the maximum aggregate fee allowed by the Company's Articles of Association of £500,000 p.a.

## Board changes in 2018

### Payments for loss of office

No payments for loss of office were made in the year.

### Payments to past directors

As set out in last year's annual report on remuneration, David Landless's Bodycote Incentive Plan (BIP) awarded in 2016 lapsed on his leaving date of 31 December 2016 and the Co-Investment Plan (CIP) awarded in 2015 has been prorated to his leaving date. Vesting of this award has occurred in line with the normal performance conditions and is set out below.

### 2015 CIP (vested on 31 May 2018)

Over the three-year period, the Group achieved absolute TSR growth of 34.1%. This performance resulted in the TSR targets being achieved at a level of 98.4%. This meant that the number of prorated shares which vested for D.F. Landless was 2,795 at a share price of £9.93 at the date of vesting on 31 May 2018.

He also received dividend equivalents in connection with the 2015 CIP amounting to £2,328.24.

### 2016 BIP

The award made to David Landless in 2016 lapsed on 31 December 2016, his leaving date.

## Directors' shareholdings

As described in Section B: Directors' Remuneration Policy, the Board operates a shareholding retention policy under which Executive Directors and other senior executives are expected, within five years of appointment, to build up a shareholding in the Company. For the purposes of this requirement, only beneficially owned shares and the net of tax value of deferred shares under the annual bonus (as they are not subject to further performance conditions) will be counted.

The shareholding requirement for the CEO is 200% of salary and for the CFO is 200% of salary (increased from 150% under our previous approved policy).

The interests in ordinary shares of directors and their connected persons as at 31 December 2018, including any interests awarded under the annual bonus, CIP or BIP, are presented below along with whether Executive Directors have met the shareholding guidelines. We note that shares under the annual bonus and the BIP are conditional on continued employment until vesting.

As at 8 March 2019, the interests of the Directors were unchanged from those at 31 December 2018.

	Counted towards the shareholding requirement		Outstanding scheme interests (not counted towards shareholding requirement)		Shareholding requirement met <sup>2</sup>
	Beneficially owned	Deferred shares granted under the annual bonus <sup>3</sup>	Shares subject to performance conditions BIP <sup>1</sup>	Shares subject to performance conditions CIP <sup>2</sup>	
<b>Executive Directors</b>					
S.C. Harris (200% minimum holding requirement)	217,121	39,560	360,247	–	Yes
D. Yates (200% minimum holding requirement)	200,000	14,013	152,840	–	Yes
<b>Non-Executive Directors (No holding requirement)</b>					
A.C. Quinn (appointed 1/1/18)	20,000	–	–	–	n/a
E. Lindqvist	12,200	–	–	–	n/a
I.B. Duncan	–	–	–	–	n/a
P. Larmon	5,000	–	–	–	n/a
L. Chahbazi (appointed 1/1/18)	–	–	–	–	n/a

1. Figures relate to unvested awards under the BIP.

2. The last CIP award took place in 2015 and vested in May 2018. There are now no shares subject to performance condition under the CIP.

3. The number of deferred shares under 2019 bonus plan can only be granted after the end of the year-end closed period and will be shown in the 2019 Annual Report. GBP value of the 2019 deferred shares are £259,852 for S. Harris and £137,952 for D. Yates.

## Summary of outstanding share awards, including share awards granted during the year – Executive Directors

The interests of the Executive Directors in the Company's share schemes as at 31 December 2018 are as follows. Note that no CIP award was made in 2016 or 2017 with the last award being granted in 2015.

		Interests as at				At 31 December 2018	Market price at award date	Market value at date of vesting	Vesting date 2018 award
		1 January 2018	Awarded in year <sup>1</sup>	Vested in year <sup>2</sup>	Lapsed in year				
Bodycote Incentive Plan (BIP)	S.C. Harris	374,023	96,911	53,317	57,370	360,247	£9.51	£9.93	March 2021
	D. Yates	82,916	69,924	–	–	152,840	£9.51	–	March 2021
Legacy Bodycote Co-Investment Plan (CIP)	S.C. Harris	5,113	–	5,031	82	–	£7.48	£9.93	May 2018

1. Mid-market closing price of a share on the day before the BIP 2018 grant was £9.51. The face value of the award to S.C. Harris was £921,624. The face value of the award to D. Yates was £664,977.

2. The 2015 BIP award did vest at 48%. The final CIP award vested during the year at 98.4% (details of the relevant performance conditions are set on page 63).

3. Retired as Group Finance Director on 1 January 2017. D. Yates appointed Chief Financial Officer on 2 January 2017. D. Yates has no awards under the legacy CIP.

## End of auditable section

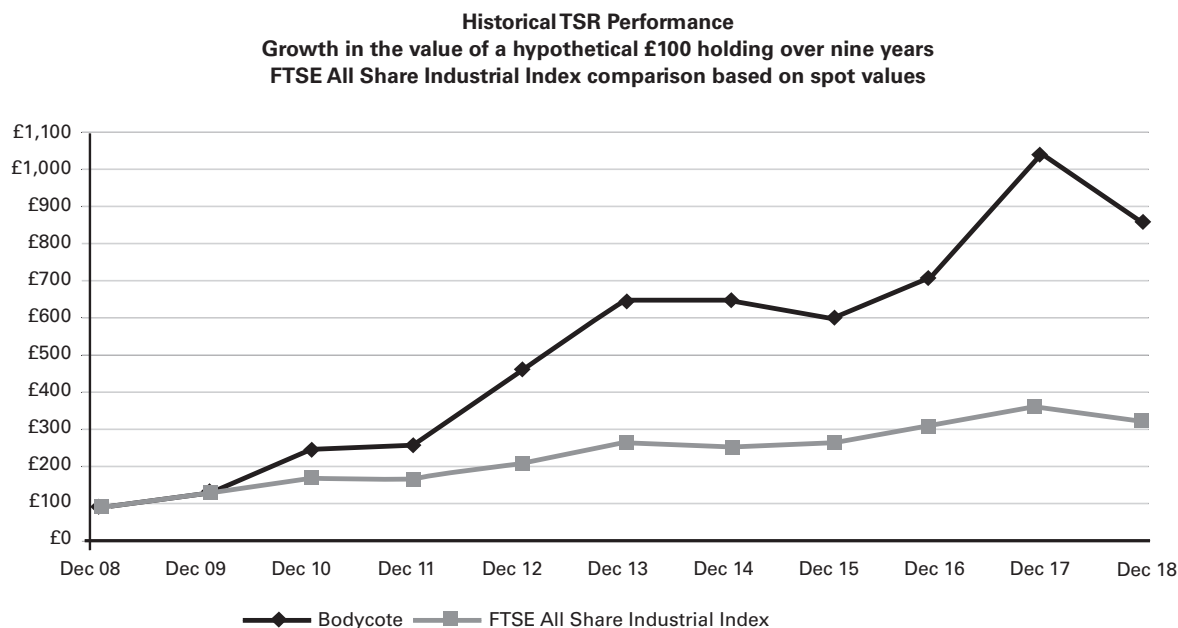
# Board report on remuneration continued

## Fees retained for external Non-Executive Directorships

To broaden the experience of Executive Directors, the position of Non-Executive Director may be held in other companies, provided that permission is sought in advance. Any external appointment must not conflict with the Directors' duties and commitments to Bodycote plc. S.C. Harris has held the position of Non-Executive Director of Mondi plc since 1 March 2011 and in accordance with Group policy he retained fees for the year of £97,174.

## Comparison of overall performance and pay

The chart below shows the value over the last nine financial years of £100 invested in Bodycote plc compared with that of £100 invested in the FTSE All Share Industrial index. The Committee has chosen this index as it is a broad market index of which Bodycote plc is a constituent and reflects the wider sector in which we operate. The points plotted represent the values at each financial year end.



The table below shows how total remuneration for the Group Chief Executive, S.C. Harris, developed over the last ten years.

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Single figure of remuneration £'000	531	906	3,252	3,840	3,089	1,803	771	875	2,280	2,649
Annual variable element award (as a % of maximum) opportunity	5%	98%	95%	73%	46%	73%	20%	19%	98%	68%
Long-term incentive vesting (as a % of maximum)	0%	0%	100%	100%	99%	44%	0%	0%	48%	89%

## Percentage change in remuneration of Group Chief Executive

The table below sets out the percentage change in the Group Chief Executive's remuneration from the prior year compared to the average percentage change in remuneration for the senior management population. The Remuneration Committee has chosen the senior management population as the wider global employee population operates under an incomparable pay structure. The senior management population is the most relevant and comparable population and is primarily based in the UK.

	Chief Executive Officer			Senior management population
	2018 (£000)	2017 (£000)	% change	Average % change
Salary	542	527	2.9%	4.7%
Annual bonus	742	1,031	-28%	7.4%*
Total	1284	1,558	-17%	5.8%*

\*Average senior management population bonus change is based on the maximum potential bonus payout.

## Relative importance of pay spend

The table below shows the total expenditure in relation to staff and employee costs and distributions to shareholders in 2017 and 2018.

	2018 £m	2017 £m	% change
Staff and employee costs	291.1	283.8	2.6%
Distributions to shareholders	81.7	30.6	166.7%

## Committee membership

During 2018 the Committee was chaired by E. Lindqvist. The Committee also comprised I.B. Duncan, P. Larmon and L. Chahbazi.

The Committee's full terms of reference are available on the Group's website. No Committee members have any personal financial interest (other than as a shareholder), conflict of interest, cross-directorships or day-to-day involvement in the running of the business. We set out below the members of the Committee, the number of meetings each Committee member attended during the year and the main responsibilities of the Committee.

## Committee activities

During 2018 the Committee met six times to consider, amongst other matters:

Theme	Agenda items
<b>Best practice</b>	<ul style="list-style-type: none"> <li>■ The Group's Remuneration Policy, discussions and feedback from the Group's AGM in 2018 and the Corporate Governance Code and Investment Management Association (IMA) guidelines on remuneration</li> <li>■ Review of the current UK corporate governance environment and the implications for the Group</li> </ul>
<b>Implementation Report</b>	<ul style="list-style-type: none"> <li>■ Consideration and approval of the Implementation Report to be put to shareholders and as summarised in Section A of the Board report on remuneration</li> </ul>
<b>Executive Directors' and senior executives' remuneration</b>	<ul style="list-style-type: none"> <li>■ Basic salaries payable to each of the Executive Directors</li> <li>■ The annual bonus and payments for the year ended 31 December 2017</li> <li>■ The annual bonus structure and performance targets for the year ended 31 December 2018</li> <li>■ The awards and vestings made under the Bodycote Incentive Plan ('BIP')</li> <li>■ The vesting made under Co-Investment Plan ('CIP') during the year</li> <li>■ Pension arrangements for senior executives</li> </ul>
<b>Reporting</b>	<ul style="list-style-type: none"> <li>■ Consideration and approval of the Board report on remuneration</li> <li>■ Feedback on shareholder consultation concerning the new Remuneration Policy and approval of the new Policy</li> </ul>

## Advisers to the Committee

The Committee was advised by PwC during 2018 on remuneration matters including providing advice on matters under consideration by the Committee, updates on good practice, legislative requirements and market practice. PwC were appointed by the Remuneration Committee in July 2015 following a competitive tender process. PwC's fees for the year, based on the quantity and complexity of the work undertaken, amounted to £51,000. PwC also undertakes tax and accounting work for the Company. PwC is a founding member of the Remuneration Consultants Group and voluntarily operates under the Code of Conduct in relation to executive remuneration consulting in the UK. The Code of Conduct can be found at remunerationconsultantsgroup.com. The Remuneration Committee is satisfied that the advice provided on executive remuneration is objective and independent, and that no conflict of interest arises as a result of these services. The Committee reviews the objectivity and independence of the advice it receives from PwC at a private meeting each year. Legal advice was provided by Eversheds. All fees are based on the quantity and complexity of work undertaken.

Following the audit tender undertaken in Q3 2018, PwC was appointed as new external auditor by the Board as of 1 January 2019. Consequently PwC resigned as Remuneration Committee consultant on 31 December 2018. The Committee has appointed E&Y as interim Remuneration Consultants as of 1 January 2019.

The Committee also received assistance from the Group Chief Executive and Group Company Secretary, although they do not participate in discussions relating to the setting of their own remuneration. The Committee in particular consulted with the Group Chief Executive and received recommendations from him in respect of his direct reports.

## Statement of shareholder voting

The table below displays the voting results on the remuneration resolution at the 2018 AGM as well as the result of the Remuneration Policy at the 2017 AGM:

	2018 Board report on remuneration (% votes)	2017 Directors' Remuneration Policy (% votes)
Votes cast	<b>79%</b>	86%
For	<b>99%</b>	96%
Against	<b>1%</b>	4%
Number of abstentions	<b>2,832,323</b>	2,034,367

### E. Lindqvist

Chair of the Remuneration Committee  
8 March 2019

# Board report on remuneration continued

## Directors' Remuneration Policy Remuneration Policy

Bodycote's Executive Remuneration Policy is to attract and motivate our senior executive team to execute our strategy and deliver value to our shareholders while ensuring the Group pays no more than is necessary.

The Policy has been revised in order to ensure continued alignment between remuneration and the evolving strategic direction of our business, as well as to ensure alignment with the new UK Corporate Governance Code.

Below is an explanation of how the Bodycote Remuneration Committee has addressed the principles prescribed by the new UK Corporate Governance Code in determining the new Executive Remuneration Policy.

### UK Corporate Governance Code Principles

### How the Committee has addressed these

**Clarity** – remuneration arrangements should be transparent and promote effective engagement with shareholders and the workforce.

The Committee is satisfied that the remuneration arrangements in the new Policy are transparent, comprising simple incentive structures that are commonplace in the market and best practice remuneration provisions.

**Simplicity** – remuneration structures should avoid complexity and their rationale and operation should be easy to understand.

No significant structural changes to incentive plans are proposed within this new Policy. The Committee concluded that the operation of the deferred Annual Bonus and Bodycote Incentive Plan (BIP) would remain easy for stakeholders to understand given the prevalence of these structures in the FTSE market and that the rationale for their operation remains unchanged and is clearly set out within the Policy.

**Risk** – remuneration arrangements should ensure reputational and other risks from excessive rewards, and behavioural risks that can arise from target-based incentive plans, are identified and mitigated.

The Committee concluded that there are two principal approaches to mitigate these risks: to ensure that remuneration arrangements do not offer the potential for excessive rewards; and to ensure the Committee has recourse to recover sums where appropriate. As such, no increases to maximum incentive opportunities are proposed in the new Policy and the malus and clawback provisions for the annual bonus and Bodycote Incentive Plan (BIP) have been extended to include a provision for the action or conduct of a participant which results in reputational damage to the Group.

**Predictability** – the range of possible values of rewards to individual directors and any other limits or discretions should be identified and explained at the time of approving the policy.

The unpredictability of company performance, including share price performance, means that the Committee cannot provide certain future values of Executive Director remuneration. However, in order to provide a guideline range of outcomes possible under the Policy, the 'illustration of application of remuneration policy' chart on page 60 indicates the potential impact of share price appreciation on Executive Director pay outcomes for both on-target and maximum performance scenarios.

**Proportionality** – the link between individual awards, the delivery of strategy and the long-term performance of the company should be clear. Outcomes should not reward poor performance.

The Committee believes that the Policy table clearly sets out how each element of remuneration links to the delivery of strategy and that the disclosure of BIP performance targets provides a clear link between individual awards and the long-term performance of the Company. The Policy also provides the Committee with discretion to adjust incentive outcomes so that reward fairly and accurately reflects the performance of the Company over the relevant period.

**Alignment to culture** – incentive schemes should drive behaviours consistent with company purpose, values and strategy.

The Committee assessed the incentive plans and considered that they were consistent with Bodycote's values:

**Honesty and Transparency:** The incentive designs are simple, transparent and in line with market practice, facilitating understanding by all stakeholders.

**Respect and responsibility:** The Committee has recourse to recover sums where appropriate.

**Creating value:** The incentives are calibrated to reward participants for delivering exceptional performance. The Committee reviews all outcomes for executive directors and has discretion to adjust outcomes where appropriate.

This Policy is intended to apply for three years from the date of the 2019 AGM and is set out below.

### Discretion

In line with the new Corporate Governance Code provision for remuneration policies to enable the use of discretion to override formulaic outcomes, the Committee has discretion in several areas of Policy as set out in this report. The Committee may also exercise operational and administrative discretions under relevant plan rules approved by shareholders as set out in those rules. In addition, the Committee has the discretion to amend Policy with regard to minor or administrative matters where it would be, in the opinion of the Committee, disproportionate to seek or await shareholder approval.

### Executive Remuneration Policy

The table below sets out the key components of Executive Directors' pay packages, including why they are used and how they are operated in practice.

### Remuneration Policy Table

Element and how it supports our strategy	Operation of the element	Maximum opportunity under the element	Performance measures
<p><b>Base salary</b>  <i>To award competitive salaries to attract and retain the talent required to execute the strategy while ensuring the Group pays no more than is necessary.</i></p>	<p>Base salaries for Executive Directors are typically reviewed annually (or more frequently if specific circumstances necessitate this) by the Committee in December each year.</p> <p>Salary levels are set and reviewed taking into account a number of factors including:</p> <ul style="list-style-type: none"> <li>■ Role, experience and performance of the executive.</li> <li>■ The Company's guidelines for salaries for all employees in the Group for the forthcoming year.</li> <li>■ The competitiveness of total remuneration assessed against FTSE 250 companies and other companies of similar size and complexity, as appropriate.</li> </ul>	<p>While the Committee has not set a maximum level of salary, ordinarily, salary increases will not exceed the average increase awarded to other Group employees.</p> <p>Increases may be above this level in certain exceptional circumstances, which may, for example, include:</p> <ul style="list-style-type: none"> <li>■ Increase in scope or responsibility.</li> <li>■ A new Executive Director who is being moved to market positioning over time.</li> </ul> <p>In general an Executive Director with the same scope and role throughout the Policy period will retain the same salary other than potential changes in line with all other Group employees.</p>	None.

## Board report on remuneration continued

Element and how it supports our strategy	Operation of the element	Maximum opportunity under the element	Performance measures
<b>Benefits</b> <i>Provides market – competitive benefits at an appropriate cost</i>	<p>The Company provides a range of cash benefits and benefits in kind to Executive Directors in line with market practice.</p> <p>These may include the provision of company car (or allowance), private medical insurance, short and long-term sick pay and death in service cover.</p> <p>The Company may also meet certain mobility costs, such as relocation support, expatriate allowances, temporary living and transportation expenses.</p> <p>Benefits provision will also extend to the reimbursement of taxable work-related expenses, such as travel.</p> <p>The provision of other benefits payable to an Executive Director is reviewed by the Committee on an annual basis to ensure appropriateness in terms of the type and level of benefits provided.</p> <p>In the case of non-UK executives, the Committee may consider providing additional allowances in line with relevant market practice, including expatriate benefits.</p>	<p>The Committee has not set a maximum level of benefit, given that the cost of certain benefits will depend on the individual's particular circumstances.</p> <p>However, benefits will be set at an appropriate level against market practice and needs for specific roles and individual circumstances.</p>	None.
<b>Pension</b> <i>Provides a market-competitive benefit in order to attract the talent required to execute the strategy and provide a market-competitive level of provision for post-retirement income</i>	<p>The Group operates a defined contribution scheme. Executive Directors are provided with a contribution to this scheme or a cash allowance of equivalent value. Base salary is the only pensionable element of remuneration.</p> <p>The same general approach applies to all employees, although contribution levels vary by seniority.</p> <p>Pension contributions for new Executive Directors are to be aligned to those applicable to other employees and will be set at the time of appointment.</p>	<p>Legacy company contribution (or cash equivalent) of up to 25% remains for current Executive Directors.</p>	None.



Element and how it supports our strategy	Operation of the element	Maximum opportunity under the element	Performance measures
<p><b>Annual bonus</b>  <i>To incentivise delivery of corporate strategy on an annual basis and reward delivery of superior performance. The deferred portion of the bonus supports longer-term shareholder alignment.</i></p>	<p>The level of bonus paid each year is determined by the Committee after the year end based on performance against targets.</p> <p>A portion of the annual bonus is paid in cash shortly after the financial year end with the remaining portion deferred for three years in Bodycote shares (see details below).</p> <p>Dividend equivalents are payable in respect of the shares which vest.</p> <p>Thirty-five per cent of any bonus earned is deferred into shares for three years, conditional on continued employment until the vesting date.</p> <p>Malus provisions apply for the duration of the performance period and to shares held under deferral.</p> <p>Clawback provisions apply to cash amounts paid for three years following payment.</p> <p>Malus and/or clawback may be applied in the following scenarios:</p> <ul style="list-style-type: none"> <li>■ Discovery of a material misstatement resulting in an adjustment in the audited accounts of the Group or any Group Company;</li> <li>■ The assessment of any performance condition or condition was based on error, or inaccurate or misleading information;</li> <li>■ The discovery that any information used to determine the cash payment under the bonus or the number of shares subject to deferral was based on error, or inaccurate or misleading information;</li> <li>■ Action or conduct of a participant which amounts to fraud or gross misconduct; or</li> <li>■ Action or conduct of a participant which results in reputational damage to the Group.</li> </ul> <p>The Committee believes that the rules of the Plan provide sufficient powers to enforce malus and clawback where required.</p>	<p>The maximum potential is 200% of base salary for the CEO and 150% of base salary for the CFO and other Executive Directors.</p> <p>At the threshold performance level there will normally be no more than 30% vesting. Awards commence vesting progressively from this point with maximum performance resulting in awards vesting in full.</p>	<p>The Committee considers the performance conditions selected for the annual bonus to appropriately support the Company's strategic objectives and provide a balance between generating profit and cash to enable the Group to pay a dividend, reward its employees and make future investments; and achieve other strategic goals to drive long-term sustainable return.</p> <p>The weighting of the measures and specific targets are reviewed on an annual basis to ensure alignment to strategy and are set to be in line with budget. Information on measures and weights that will apply for specific years will be included in the relevant year's Annual Report on Remuneration.</p> <p>At least 70% of the bonus will be based on the achievement of Group financial targets.</p> <p>The Committee retains discretion in exceptional circumstances to change performance measures and targets and the weightings attached to performance measures part way through a performance year if there is a significant and material event which causes the Committee to believe the original measures, weightings and targets are no longer appropriate.</p> <p>Discretion may also be exercised in cases where the Committee believe that the bonus outcome is not a fair and accurate reflection of business performance. The exercise of this discretion may result in a downward or upward movement in the amount of bonus earned resulting from the application of the performance measures.</p> <p>Any adjustments or discretion applied by the Committee will be fully disclosed in the following year's Remuneration Report.</p> <p>The Committee is of the opinion that given the commercial sensitivity arising in relation to the detailed financial targets used for the annual bonus, disclosing precise targets for the annual bonus plan in advance would not be in shareholder interests. Actual targets, performance achieved and awards made will be published at the end of the performance periods so shareholders can fully assess the basis for any pay-outs under the annual bonus.</p>

# Board report on remuneration continued

Element and how it supports our strategy	Operation of the element	Maximum opportunity under the element	Performance measures
<p><b>Bodycote Incentive Plan (BIP) 2016</b>  <i>To incentivise delivery of long-term strategic goals and shareholder value and aid retention of senior management.</i></p>	<p>Awards will be granted annually under the Bodycote Incentive Plan subject to a three year vesting period and stretching performance conditions measured over three years. Awards granted from 2019 will also have a two-year holding period from the date of vest.</p> <p>Dividend equivalents are payable in respect of the shares which vest.</p> <p>The Committee retains the discretion in exceptional circumstances to adjust the vesting outcome or the targets for awards as long as the adjusted targets are no less stretching. In such an event the Committee will consult with major shareholders and will clearly explain the rationale for the changes in the report on remuneration.</p> <p>Discretion may also be exercised in cases where the Committee believes that the outcome is not a fair and accurate reflection of business performance. The exercise of this discretion may result in a downward or upward movement in the amount of the LTIP vesting resulting from the application of the performance measures.</p> <p>Malus provisions apply for the duration of the performance period.</p> <p>Clawback provisions apply to amounts for two years following vesting.</p> <p>Malus and/or clawback may be applied in the following scenarios:</p> <ul style="list-style-type: none"> <li>■ Discovery of a material misstatement resulting in an adjustment in the audited accounts of the Group or any Group Company;</li> <li>■ The assessment of any performance condition or condition was based on error, or inaccurate or misleading information;</li> <li>■ The discovery that any information used to determine the number of shares subject to an award was based on error, or inaccurate or misleading information;</li> <li>■ Action or conduct of a participant which amounts to fraud or gross misconduct; or</li> <li>■ Action or conduct of a participant which results in reputational damage to the Group.</li> </ul> <p>The Committee believes that the rules of the Plan provide sufficient powers to enforce malus and clawback where required.</p>	<p>The maximum face value of an award which may be granted under the Plan in any year is up to 175% of base salary for the Executive Directors.</p> <p>At the threshold performance level there will normally be no more than 0% vesting. Awards commence vesting progressively from this point with maximum performance resulting in awards vesting in full.</p>	<p>Awards vest based on performance over three years against performance measures chosen by the Committee to align with business and strategic priorities.</p> <p>The measures for Executive Directors are:</p> <ul style="list-style-type: none"> <li>■ 50% ROCE</li> <li>■ 50% headline EPS</li> </ul> <p>In addition, the vesting of awards may only occur if headline EPS is above a defined hurdle level.</p> <p>The Committee considers these performance conditions selected for the BIP to currently appropriately underpin the Company's strategic objectives. Due to the nature of the Company's activities the Committee consider ROCE to provide shareholders with an appropriate measure of how well the Company is performing and is being managed, while headline EPS provides a measure of the level of value created for shareholders. ROCE and headline EPS are our top two KPIs as shown on page 2 of the Annual Report.</p> <p>The Committee may adjust the performance measures attaching to awards and the weighting of these measures if it feels this will create greater alignment with business and strategic priorities.</p> <p>A significant change to the measures used would only be adopted following consultation with major shareholders.</p> <p>The targets for the performance measures are reviewed on an annual basis to ensure alignment to strategy and are set to be in line with budget. Details of performance targets will be included in the relevant year's Annual Report on Remuneration.</p>

Element and how it supports our strategy	Operation of the element	Maximum opportunity under the element	Performance measures
<b>Shareholding requirement</b> <i>To provide alignment of interest between participants and shareholders.</i>	<p>The Board operates a shareholding retention policy under which Executive Directors are expected, within five years from appointment, to build up a shareholding in the Company.</p> <p>The Committee has the power to introduce a post cessation of employment minimum shareholding requirement in line with the UK Corporate Governance Code and will review emerging market practice before determining the extent of any terms or conditions of any requirements.</p>	Executive Directors are required to build up a holding of 200% of base salary.	None.

### Notes to the Remuneration Policy Table

The Committee reserves the right to make any remuneration payments and payments for loss of office notwithstanding that they are not in line with the Policy set out on pages 68 to 77 where the terms of the payment were agreed (i) before the Policy came into effect or (ii) at a time when the relevant individual was not a Director of the Company and, in the opinion of the Committee, the payment was not in consideration for the individual becoming a Director of the Company. For these purposes 'payments' include the Committee satisfying awards of variable remuneration and, in relation to an award over shares, the terms of the payment being 'agreed' at the time the award is granted.

Executive Directors' remuneration is reviewed annually and takes into account a number of factors. The Company adopts a policy of positioning fixed pay for all its employees at a level which is competitive to market but which does not require the Company to pay any more than is necessary. Senior and high performing individuals at all levels and across all functions within the organisation are invited to participate in both annual and long-term incentive arrangements, which are similar to those offered to the Executive Directors to ensure reward strategy is calibrated to provide substantive reward only on achievement of superior performance.

### Non-Executive Director (NED) Fee Policy

The Policy on Non-Executive Director (NED) and Chair fees is set out below.

Element and how it supports our strategy	Operation of the element	Maximum opportunity under the element	Performance measures
<b>Fees for Non-Executive Directors</b> <i>To attract NEDs who have a broad range of experience and skills to oversee the implementation of our strategy.</i>	<p>The fees for the Non-Executives are determined by the Chair and the Group Chief Executive.</p> <p>The fee for the Chair is set by the Remuneration Committee.</p> <p>The Chair and Non-Executive fees are reviewed on an annual basis. When reviewing fees, the primary source of comparative market data is FTSE 250 companies and other companies of similar size and complexity, as appropriate.</p> <p>The fees for the Chair and Non-Executives are set at a level that will attract individuals with the necessary experience and ability to make a significant contribution to the Group's affairs. The fees reflect the time commitment and responsibilities of the roles.</p> <p>The Chair and Non-Executive Directors are not entitled to any pension or other employment benefits and, in line with the UK Corporate Governance Code, are not allowed to participate in any incentive plan.</p> <p>The Company will pay reasonable expenses incurred by the Non-Executive Directors and Chair and may settle any tax incurred in relation to these.</p>	<p>Fees for Non-Executive Directors for the following year are set out in the statement of implementation of Policy on page 59.</p> <p>The Company's Policy is that the Chair and Non-Executive Directors receive a fixed fee for their services as members of the Board and its Committees. The fee structure may also include additional fees for chairing a Board Committee and/or further responsibilities (for example, Senior Independent Directorship).</p>	None.

# Board report on remuneration continued

## Fees retained for External Non-Executive Directorships

To broaden the experience of Executive Directors, they may hold positions in other companies as Non-Executive Directors provided that permission is sought in advance. Any external appointment must not conflict with the Directors' duties and commitments to Bodycote plc.

## Statement of consideration of employment conditions elsewhere in the Group

The Company adopts a policy of positioning fixed pay for all its employees at a level which is competitive to the market but which does not require the Company to pay any more than is necessary. Senior and high-performing individuals at all levels and across all functions within the organisation are invited to participate in both annual and long-term incentive arrangements, similar to the executive directors to ensure reward strategy is calibrated to provide substantive reward only on achievement of superior performance.

The Committee does not consult directly with employees when formulating Executive Director pay policies. However, it does take into account information provided by the Human Resources function on pay and conditions across the Company, and considers these as part of its discussions and decision making, along with feedback from employee satisfaction surveys. In addition, the Board of Bodycote is developing its approach to engagement with the workforce in line with the guidance in the new Corporate Governance Code and the results of this engagement will be available to the Remuneration Committee.

We recognise the Government's recent commentary in this area, and will ensure that our approach to consideration of employee views and pay and conditions across the Company reflect appropriate legislative and corporate governance requirements.

## Statement of consideration of Shareholders' Views

The Committee always welcomes the views of shareholders in respect of pay policy as well as those views expressed on behalf of shareholders by their respective proxy advisers. The Committee documents all remuneration related comments made at the Company's AGM and feedback received during consultation with shareholders throughout the year. Any feedback received is fully considered by the Committee.

In developing the proposed Remuneration Policy for 2019 and beyond the Remuneration Committee engaged extensively with the Company's key shareholders and their representative bodies. Through this process the Remuneration Committee took on board the feedback received and refined the proposed Remuneration Policy as appropriate to ensure it meets the expectations of our shareholders.

## Approach to Recruitment Remuneration

When recruiting new Executive Directors, the Company's Policy is to pay what is necessary to attract individuals with the skills and experience appropriate to the role to be filled, taking into account remuneration across the Group, including other senior executives, and that offered by other FTSE 250 companies and other companies of similar size and complexity. New Executive Directors will generally be appointed on remuneration packages with the same structure and pay elements as described in the Policy table on pages 68 to 77.

Component	Policy
<b>General</b>	<p>The Company's Policy is to pay what is necessary to attract individuals with the skills and experience appropriate to the role to be filled.</p> <p>The initial notice period may be longer than the Company's one year policy (up to a maximum of two years). However, this will reduce by one month for every month served, until the Company's Policy position is reached.</p>
<b>Base salary</b>	<p>Base salary levels will be set at an appropriate level to recruit the best candidate in consideration of the new recruit's existing salary, location, skills and experience and expected contribution to the new role, the current salaries of other Executive Directors in the Company and current market levels for the role.</p>
<b>Other benefits</b>	<p>Other benefits will be considered in light of the Policy in place for the other Executive Director(s). If it is in the best interests of the Company and shareholders, the Committee may consider providing additional benefits.</p>
<b>Pension</b>	<p>Pension contribution levels will be considered by the Committee in light of the new recruit's package as a whole, market practice at the time and in line with the new provision that Executive Director pension contributions will be in line with Bodycote contribution rates applicable to other employees.</p>
<b>Annual bonus</b>	<p>Normal awards will be made under the annual bonus plan in line with the Remuneration Policy. The Executive Director may be invited to participate in the bonus on a prorated basis in the first year of appointment.</p>
<b>Long-term incentives</b>	<p>Normal awards will be made under the BIP in line with the Remuneration Policy. The Executive Director may be invited to participate in 'in flight' BIP awards on a prorated basis when appointed.</p> <p>The Company is required to set out the maximum amount of variable pay which could be paid to a new Director in respect of his/her recruitment. In order to provide the Company with sufficient flexibility in a recruitment scenario, the Committee has set this figure as 450% of base salary. This covers the maximum annual bonus and the maximum face value of any long-term incentive awards. This level of variable pay would only be available in exceptional circumstances, and in order to achieve such a level of variable pay, stretching targets would need to be met. For the avoidance of doubt, this 450% variable pay limit excludes the value of any 'buyout' payments or awards associated with forfeited awards.</p>

Component	Policy
<b>Replacement awards</b>	For an external appointment, although there are no plans to offer additional cash and/or share-based payments on recruitment, the Committee reserves the right to do so when it considers this to be in the best interests of the Company and shareholders. Such payments may take into account remuneration relinquished when leaving the former employer and would reflect the nature, time horizons and performance requirements attached to that remuneration. Shareholders will be informed of any such payments at the time of appointment. The Committee may make awards on hiring an external candidate to 'buyout' awards which will be forfeited on leaving the previous employer. Our approach to this is to carry out a detailed review of the awards which the individual will lose and calculate the estimated value of them. In doing so, we will consider the vesting period, the option exercise period if applicable, whether the awards are cash or share based, performance related or not, the company's recent performance and payout levels and any other factors we consider appropriate. If a buyout award is to be made, the structure and level will be carefully designed and will generally reflect and replicate the previous awards as accurately as possible. We will make the award subject to appropriate malus and clawback provisions in the event that the individual resigns or is summarily terminated within a certain time frame. An explanation will be provided at the time of recruitment of why a buyout award has been granted.
<b>Internal promotions</b>	For internal promotions any commitments made prior to appointment may continue to be honoured as the executive is transitioned to the new remuneration arrangements.

Shareholders will be informed of any Director appointment and the individual's remuneration arrangements as soon as practicable following the appointment.

Fee levels for a new Chair or new Non-Executive Directors will be determined in accordance with the Policy set out on page 73.

### Service Contracts

All Directors' service contracts and letters of appointment are available for inspection at the Company's registered office.

A summary of the key terms of the Executive Directors' service contracts is set out below:

	<b>S.C. Harris, Group Chief Executive</b>	<b>D. Yates, Chief Financial Officer</b>
<b>Date of service contract</b>	6 October 2008	1 November 2016
<b>Notice period</b>	12 months	12 months
<b>Remuneration</b>	<ul style="list-style-type: none"> <li>■ Annual base salary</li> <li>■ Potential for cash in lieu of pension</li> <li>■ Reimbursement of expenses (if satisfactory evidence provided)</li> <li>■ Private medical insurance</li> <li>■ Company car allowance</li> <li>■ Entitlement to receive an annual performance-related bonus award</li> <li>■ Entitlement to participate in a long-term incentive plan</li> </ul>	<ul style="list-style-type: none"> <li>■ Annual base salary</li> <li>■ Potential for cash in lieu of pension</li> <li>■ Reimbursement of expenses (if satisfactory evidence provided)</li> <li>■ Private medical insurance</li> <li>■ Company car allowance</li> <li>■ Entitlement to receive an annual performance-related bonus award</li> <li>■ Entitlement to participate in a long-term incentive plan</li> <li>■ Entitlement to a reasonable relocation package if D. Yates relocates within 30 months of starting date of 1 November 2016</li> </ul>
<b>Termination</b>	Company has right to terminate on payment of a termination payment with agreement of executive	Company has right to terminate on payment of a termination payment
<b>Non-competition</b>	During employment and for 12 months thereafter	During employment and for 12 months thereafter

Other than the contents of the contracts, there are no obligations that may give rise to remuneration.

Director	Date of appointment	Notice period
P. Larmon	13 September 2016	6 months
E. Lindqvist	1 June 2012	6 months
I.B. Duncan	17 November 2014	6 months
A.C. Quinn	1 January 2018	6 months
L. Chahbazi	1 January 2018	6 months

The Non-Executive Directors of the Company (including the Chair) do not have service contracts. The Non-Executive Directors are appointed by letters of appointment. Each independent Non-Executive Director's term of office runs for a maximum three year period.

# Board report on remuneration continued

The initial terms of the Non-Executive Directors' positions are subject to their re-election by the Company's shareholders at the next AGM and to re-election at any subsequent AGM at which the Non-Executive Directors stand for re-election. All Directors will be put forward for re-election by shareholders on an annual basis.

## Termination Remuneration Policy

It is the Company's Policy that Executive Directors have service contracts with a one-year notice period and terminable by one year's notice by the employer at any time, and by payment of one year's basic salary and other fixed benefits in lieu of notice by the employer. All future appointments to the Board will comply with this requirement.

The Committee will honour Executive Directors' contractual entitlements. Service contracts do not contain liquidated damages clauses. If a contract is to be terminated, the Committee will determine such mitigation as it considers fair and reasonable in each case. There are no contractual arrangements that would guarantee a pension with limited or no abatement on severance or early retirement. There is no agreement between the Company and its Executive Directors or employees, providing for compensation for loss of office or employment that occurs because of a takeover bid.

Component	Policy
<b>Compensation for loss of office in service contracts</b>	<p>Under the terms of the Chief Executive's contract, the Company may at its choice, in lieu of giving notice, terminate his service contract by making a payment equivalent to: one year's annual base salary, 25% of base salary in respect of all other remuneration and benefits (other than annual bonus and incentives) and annual bonus equal to the average bonus paid up to three years prior to the date of notice. For the purposes of transparency, if the CEO had left Bodycote in FY18, and the Company had chosen to make a compensation payment in lieu of giving notice, this would have comprised: £541,923 (one year of base salary) + £135,481 (25% of base salary) + £450,667 (three year average bonus over FY15-FY17) = £1,128,070.</p> <p>Under the terms of the Chief Financial Officer's contract, the contract is terminable by one year's notice by the employer at any time, and by payment of one year's basic salary and other fixed benefits in lieu of notice by the employer.</p>
<b>Treatment of cash element of the bonus under Plan rules</b>	<p>If termination is by way of death, injury, illness, disability, redundancy, retirement or any other circumstances the Committee determines (a 'good leaver'), the level of bonus will be measured at the bonus measurement date. Bonus will normally be prorated for the period worked during the financial year.</p> <p>The Committee retains the discretion:</p> <ul style="list-style-type: none"><li>■ to determine that an Executive is a good leaver. It is the Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders;</li><li>■ not to prorate the bonus to time. The Committee's Policy is that it will prorate bonus for time. It is the Committee's intention to use its discretion to not prorate in circumstances where there is an appropriate business case which will be explained in full to shareholders.</li></ul> <p>Under all other circumstances no bonus will be earned on cessation of employment (other than set out above in the legacy arrangements for the CEO).</p>
<b>Treatment of unvested deferred bonus awards under Plan rules</b>	<p>If termination is by way of death, injury, illness, disability, redundancy, retirement or any other circumstances the Committee determines (a 'good leaver'), deferred shares may be released to the participant at the normal vesting date.</p> <p>Under all other circumstances unvested awards will lapse on cessation of employment.</p> <p>The Committee has the following elements of discretion:</p> <ul style="list-style-type: none"><li>■ to determine that an Executive is a good leaver. It is the Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders;</li><li>■ to vest deferred shares at the end of the original deferral period or at the date of cessation. The Committee's Policy is that shares will vest on the original date of vesting. The Committee will make this determination depending on the type of good leaver reason resulting in the cessation.</li></ul>

Component	Policy
<b>Treatment of unvested BIP 2016</b>	<p>On cessation of employment, awards under the BIP will lapse in full, unless the Committee determines that the individual is a good leaver (see above for definition). In instances where the Committee determines that award should not lapse in full, awards will normally vest at the normal vesting date, prorated for time served and subject to the achievement of the original performance conditions.</p> <p>The Committee has the following elements of discretion:</p> <ul style="list-style-type: none"> <li>■ to determine that an Executive is a good leaver. It is the Committee's intention to only use this discretion in circumstances where there is an appropriate business case which will be explained in full to shareholders;</li> <li>■ to measure performance over the original performance period or at the date of cessation. The Committee will make this determination depending on the type of good leaver reason resulting in the cessation; and</li> <li>■ to prorate the maximum number of shares to the time from the date of grant to the date of cessation. The Committee's policy is that it will prorate awards for time. It is the Committee's intention to use discretion to not prorate in circumstances where there is an appropriate business case which will be explained in full to shareholders.</li> </ul> <p>In addition, awards granted from 2019 will be subject to a two-year holding period.</p>
<b>Exercise of discretion</b>	<p>In the event that an Executive Director leaves the Company, the Committee's policy for exit payments is to consider the reasons for cessation and consequently whether any exit payments other than those contractually required are warranted.</p> <p>Further, in the event of a compromise or settlement agreement, the Committee may agree payments it considers reasonable in settlement of legal claims. This may include an entitlement to compensation in respect of their statutory rights under employment protection legislation in the UK or in other jurisdictions. The Committee may also include in such payments reasonable reimbursement of professional fees in connection with such agreements.</p>
<b>Change of control</b>	<p>On change of control the awards under the Company's incentive plans will generally vest subject to performance and time apportionment as determined by the Committee and in accordance with the rules of the relevant Plan.</p>

The remuneration package for the Executive Directors is designed to provide an appropriate balance between fixed and variable performance-related components. The Committee is satisfied that the composition and structure of the remuneration package is appropriate, clearly supports the Company's strategic ambitions and does not incentivise inappropriate risk taking and reviews this on an annual basis.

# Directors' responsibilities statement

## Responsibility of directors for the preparation of the Annual Report and financial statements

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and Article 4 of the IAS Regulation and have elected to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law), including FRS 101 'Reduced Disclosure Framework'. Under company law the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period.

In preparing the Parent Company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

In preparing the Group financial statements, International Accounting Standard 1 requires that directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the Company's ability to continue as a going concern.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

## Responsibility statement of the directors in respect of the Annual Report and financial statements

We confirm that to the best of our knowledge:

- the financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- the strategic report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- the annual report and financial statements, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's performance, business model and strategy.

This responsibility statement was approved by the Board of directors on 7 March 2019 and is signed on its behalf by:

**S.C. Harris**  
Group Chief Executive  
8 March 2019

**D. Yates**  
Chief Financial Officer  
8 March 2019



# Independent auditor's report

## To the Members of Bodycote plc

### Report on the audit of the financial statements

#### Opinion

In our opinion:

- the financial statements of Bodycote plc (the 'parent company') and its subsidiaries (the 'group') give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2018 and of the group's profit for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 101 "Reduced Disclosure Framework" and;
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements which comprise:

- the Consolidated Income Statement;
- the Consolidated Statement of Comprehensive Income;
- the Consolidated and Parent Company Statements of Financial Position;
- the Consolidated Cash Flow Statement;
- the Consolidated and Parent Company Statements of Changes in Equity;
- the Group and Company Accounting Policies;
- the related notes 1 to 30 to the Group financial statements; and
- the related notes 1 to 12 to the Parent Company financial statements.

The financial reporting framework that has been applied in the preparation of the group financial statements is applicable law and IFRSs as adopted by the European Union. The financial reporting framework that has been applied in the preparation of the parent company financial statements is applicable law and United Kingdom Accounting Standards, including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

#### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the group and the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard as applied to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We confirm that the non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### Summary of our audit approach

<b>Key audit matters</b>	The key audit matters that we identified in the current year were: <ul style="list-style-type: none"><li>■ <i>Taxation accounting – valuation of specific uncertain tax provisions</i></li><li>■ <i>Revenue recognition – manual adjustments to revenue</i></li></ul>
<b>Materiality</b>	The materiality that we used for the group financial statements was £6.6 million which was determined on the basis of 5% of statutory pre-tax profit.
<b>Scoping</b>	As a consequence of the audit scope determined, we achieved coverage of approximately 74% of revenue, 75% of profit before tax and 77% of net assets
<b>Significant changes in our approach</b>	<p>Our approach is consistent with the previous year with the exception of the removal of impairment of goodwill and intangibles and pension liability assumptions as key audit matters for the 2018 audit report.</p> <p>In 2018 we no longer consider the impairment of goodwill and intangible assets to be a key audit matter. This assessment is based on our risk assessment procedures and the forecast performance of the Group's cash generating units ('CGUs').</p> <p>We also no longer consider the pension liability assumptions underpinning the UK defined benefit pension scheme to be a key audit matter. This follows considerations of the nature of the pension scheme and historical experience of testing of the scheme liability assumptions</p>

# Independent auditor's report continued

To the Members of Bodycote plc

## Conclusions relating to going concern, principal risks and viability statement

### Going concern

We have reviewed the directors' statement on page 28 to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the group's and company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements.

We considered as part of our risk assessment the nature of the group, its business model and related risks including where relevant the impact of Brexit, the requirements of the applicable financial reporting framework and the system of internal control. We evaluated the directors' assessment of the group's ability to continue as a going concern, including challenging the underlying data and key assumptions used to make the assessment, and evaluated the directors' plans for future actions in relation to their going concern assessment.

We are required to state whether we have anything material to add or draw attention to in relation to that statement required by Listing Rule 9.8.6R(3) and report if the statement is materially inconsistent with our knowledge obtained in the audit.

**We confirm that we have nothing material to report, add or draw attention to in respect of these matters.**

### Principal risks and viability statement

Based solely on reading the directors' statements and considering whether they were consistent with the knowledge we obtained in the course of the audit, including the knowledge obtained in the evaluation of the directors' assessment of the group's and the company's ability to continue as a going concern, we are required to state whether we have anything material to add or draw attention to in relation to:

- the disclosures on pages 29-33 that describe the principal risks and explain how they are being managed or mitigated;
- the directors' confirmation on page 78 that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity; or
- the directors' explanation on page 28 as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We are also required to report whether the directors' statement relating to the prospects of the group required by Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.

**We confirm that we have nothing material to report, add or draw attention to in respect of these matters.**

## Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team.

These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

## Taxation – valuation of specific uncertain tax provisions

### Key audit matter description



As described in note 6 and the Group's accounting policies, the Group recognises a number of tax provisions in respect of ongoing tax inquiries and reflecting the multinational tax environment in which the Group operates. These provisions total £16.1 million (2017: £17.5 million).

The tax risk concerns the judgements and estimates applied in the determination of provisions for liabilities attributed to specific uncertain tax provisions linked to the Group's corporate arrangements.

This is described as an area of focus in the Report of the Audit Committee

### How the scope of our audit responded to the key audit matter



In conjunction with our taxation audit specialists, we performed the following audit procedures in order to address this risk:

- Assessed the design and implementation of the controls in place to address the key audit matter;
- Assessed the assumptions and judgements concerning the adequacy of specific uncertain tax provisions by challenging management's assumptions; and
- Reviewed the available correspondence from the various tax authorities and drawing on the experience of our taxation specialists in respect of similar situations.

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**Key observations**

From the work performed above we are satisfied that the provisions held on the balance sheet for specific uncertain tax provisions are reasonable.

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**Revenue recognition - manual adjustments to revenue** **Key audit matter description**

When assessing the potential risk of fraud in relation to revenue recognition, we have considered the nature of the automated and manual transactions recorded across the Group, considering the typical sales cycle for the services provided by the Group as described in the Group's accounting policies. Following which we have determined that a key audit matter in relation to fraud exists relating to the risk of inappropriate manual adjustments being recorded in revenue. This is because the value of manual journals is material in total, and due to the risk of management override in this area.

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**How the scope of our audit responded to the key audit matter**

We performed the following audit procedures in order to address this risk:

- Assessed the design and implementation of the controls in place to address the key audit matter;
  - Tested the completeness and accuracy of the transactions listings split between automated and manual journal types;
  - Performed procedures to understand the nature of the manual adjustments arising; and
  - Selected a sample of manual entries posted throughout the year and obtained the relevant supporting documentation in order to validate that journal postings were accurate and had commercial substance.
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**Key observations**

From the work performed we have not noted any manual adjustments to revenue that we would not expect in the usual course of business, or that cannot be supported.

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# Independent auditor's report continued

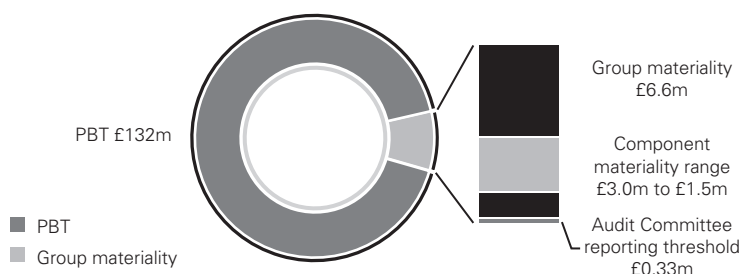
## To the Members of Bodycote plc

### Our application of materiality

We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
<b>Materiality</b>	£6.6 million (2017: £5.6 million)	£4.2 million (2017: £4.5 million)
<b>Basis for determining materiality</b>	5% of statutory pre-tax profit (2017: 5% of expected statutory pre-tax profit)	The parent company materiality represents approximately 1% (2017: 1%) of equity.
<b>Rationale for the benchmark applied</b>	Pre-tax profit is determined to be the most stable basis of underlying business performance.	As a non-trading parent company, equity is the key driver of the company



We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.33 million (2017: £0.28 million), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

### An overview of the scope of our audit

Our Group audit was scoped by obtaining an understanding of the Group and its environment, including group-wide controls, and assessing the risks of material misstatement at the Group level.

Based on this assessment, we focused our Group audit scope primarily on the audit work relating to 22 components covering the US shared service centre, the European shared service centre, UK, France and Turkey. One component within Czech Republic was removed from Group scope as part of our risk assessment process to pinpoint our focus and attention to material components where the key audit matters and judgements affecting the Group financial statements are expected. The parent company is located in the UK and audited directly by the Group audit team.

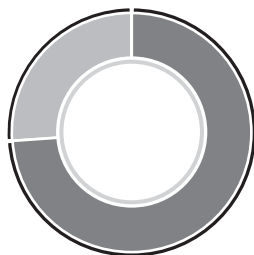
As a consequence of the audit scope determined, we achieved coverage of approximately 74% (2017: 73%) of revenue, 75% (2017: 78%) of profit before tax and 77% (2017: 79%) of net assets. Our audit work at each component was executed at levels of materiality applicable to each individual component which were lower than Group materiality. Component materiality, excluding the parent company, ranged from £1.5m to £3.0m (2017: £1.5m to £2.8m).

The Group audit team have designed the audit procedures for all significant risks to be addressed by the component auditors and issued Group referral instructions detailing the nature and form of the reporting required. The Group audit team continued to follow a program of planned visits that has been designed so that a senior member of the Group audit team visits each of the significant finance function locations included as full scope for the Group audit on a rotational basis. During the year, senior members of the Group audit team have visited the US shared service centre, the European shared service centre, and France.

In years when we do not visit a material component we include the component audit team in our team briefing, discuss their risk assessment, attend close meetings by conference call and review documentation of the findings from their work.

At the parent entity level we also tested the consolidation process and carried out analytical procedures to confirm our conclusion that there were no significant risks of material misstatement of the aggregated financial information of the remaining components not subject to audit or audit of specified account balances.

#### Revenue



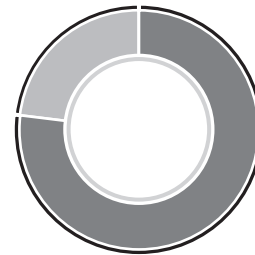
■ Full audit scope 74%  
■ Review at Group level 26%

#### Profit before tax



■ Full audit scope 75%  
■ Review at Group level 25%

#### Net assets



■ Full audit scope 77%  
■ Review at Group level 23%

# Independent auditor's report continued

## To the Members of Bodycote plc

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### Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

In this context, matters that we are specifically required to report to you as uncorrected material misstatements of the other information include where we conclude that:

- *Fair, balanced and understandable – the statement given by the directors that they consider the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the group's position and performance, business model and strategy, is materially inconsistent with our knowledge obtained in the audit; or*
- *Audit committee reporting – the section describing the work of the audit committee does not appropriately address matters communicated by us to the audit committee; or*
- *Directors' statement of compliance with the UK Corporate Governance Code – the parts of the directors' statement required under the Listing Rules relating to the company's compliance with the UK Corporate Governance Code containing provisions specified for review by the auditor in accordance with Listing Rule 9.8.10R(2) do not properly disclose a departure from a relevant provision of the UK Corporate Governance Code.*

**We have nothing to report in respect of these matters.**

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### Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

### Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud are set out below.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: [www.frc.org.uk/auditorsresponsibilities](http://www.frc.org.uk/auditorsresponsibilities). This description forms part of our auditor's report.

## Extent to which the audit was considered capable of detecting irregularities, including fraud

We identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and then design and perform audit procedures responsive to those risks, including obtaining audit evidence that is sufficient and appropriate to provide a basis for our opinion.

### Identifying and assessing potential risks related to irregularities

In identifying and assessing risks of material misstatement in respect of irregularities, including fraud and non-compliance with laws and regulations, our procedures included the following:

- enquiring of management, internal audit and the audit committee, including obtaining and reviewing supporting documentation, concerning the group's policies and procedures relating to:
  - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
  - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
  - the internal controls established to mitigate risks related to fraud or non-compliance with laws and regulations;
- discussing among the engagement team, including material component audit teams, and involving relevant internal specialists, including tax, valuations, pensions and IT, specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud; and
- obtaining an understanding of the legal and regulatory frameworks that the group operates in, focusing on those laws and regulations that had a direct effect on the financial statements or that had a fundamental effect on the operations of the group. The key laws and regulations we considered in this context included the UK Companies Act, Listing Rules, pensions and tax legislation.

### Audit response to risks identified

As a result of performing the above, we identified manual adjustments to revenue and valuation of specific uncertain tax provisions as key audit matters. The key audit matters section of our report explains the matters in more detail and also describes the specific procedures we performed in response to those key audit matters.

In addition to the above, our procedures to respond to risks identified included the following:

- reviewing the financial statement disclosures and testing to supporting documentation to assess compliance with relevant laws and regulations discussed above;
- enquiring of management, the audit committee and in-house / external legal counsel concerning actual and potential litigation and claims;
- performing analytical procedures to identify any unusual or unexpected relationships that may indicate risks of material misstatement due to fraud;
- reading minutes of meetings of those charged with governance, reviewing internal audit reports and reviewing correspondence with HMRC; and
- in addressing the risk of fraud through management override of controls, testing the appropriateness of journal entries and other adjustments; assessing whether the judgements made in making accounting estimates are indicative of a potential bias; and evaluating the business rationale of any significant transactions that are unusual or outside the normal course of business.

We also communicated relevant identified laws and regulations and potential fraud risks to all engagement team members including internal specialists, and remained alert to any indications of fraud or non-compliance with laws and regulations throughout the audit.

## Report on other legal and regulatory requirements

### Opinions on other matters prescribed by the Companies Act 2006

In our opinion the part of the directors' remuneration report to be audited has been properly prepared in accordance with the Companies Act 2006.

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements

In the light of the knowledge and understanding of the group and of the parent company and their environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

# Independent auditor's report continued

To the Members of Bodycote plc

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## Matters on which we are required to report by exception

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### Adequacy of explanations received and accounting records

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- The parent company financial statements are not in agreement with the accounting records and returns.

**We have nothing to report in respect of these matters.**

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### Directors' remuneration

Under the Companies Act 2006 we are also required to report if in our opinion certain disclosures of directors' remuneration have not been made or the part of the directors' remuneration report to be audited is not in agreement with the accounting records and returns.

**We have nothing to report in respect of these matters.**

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### Other matters

#### Auditor tenure

Following the recommendation of the audit committee, we were appointed by the Board of Directors in 2002 to audit the financial statements for the year ending 31 December 2003 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is 16 years, covering the years ending 31 December 2003 to 31 December 2018.

#### Consistency of the audit report with the additional report to the audit committee

Our audit opinion is consistent with the additional report to the audit committee we are required to provide in accordance with ISAs (UK).

#### Use of our report

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Mark Mullins, FCA (Senior statutory auditor)

for and on behalf of Deloitte LLP  
Statutory Auditor  
London, United Kingdom  
8 March 2019



# Consolidated income statement

For the year ended 31 December 2018

	Note	2018 £m	2017 £m
<b>Revenue</b>	2	<b>728.6</b>	690.2
Cost of sales and overheads		<b>(594.5)</b>	(570.8)
<b>Operating profit</b>	2,3	<b>134.1</b>	119.4
Investment revenue		<b>0.2</b>	0.1
Finance costs	5	<b>(2.1)</b>	(2.5)
<b>Profit before taxation</b>		<b>132.2</b>	117.0
Tax impact in relation to prior year change in US tax rate		<b>-</b>	6.4
Taxation		<b>(28.6)</b>	(26.1)
Taxation charge	6	<b>(28.6)</b>	(19.7)
<b>Profit for the year</b>		<b>103.6</b>	97.3
Attributable to:			
Equity holders of the parent		<b>103.2</b>	97.1
Non-controlling interests		<b>0.4</b>	0.2
		<b>103.6</b>	97.3
<b>Earnings per share</b>	8	<b>Pence</b>	Pence
Basic		<b>54.2</b>	51.0
Diluted		<b>54.2</b>	51.0

All activities have arisen from continuing operations.

# Consolidated statement of comprehensive income

For the year ended 31 December 2018

	2018 £m	2017 £m
<b>Profit for the year</b>	<b>103.6</b>	97.3
<b>Items that will not be reclassified to profit or loss:</b>		
Actuarial (loss)/gain on defined benefit pension schemes	<b>(0.8)</b>	6.7
Tax on items not reclassified	<b>(0.5)</b>	(1.0)
<b>Total items that will not be reclassified to profit or loss</b>	<b>(1.3)</b>	5.7
<b>Items that may be reclassified subsequently to profit or loss:</b>		
Exchange gains/(losses) on translation of foreign operations	<b>15.8</b>	(11.7)
<b>Total items that may be reclassified subsequently to profit or loss</b>	<b>15.8</b>	(11.7)
<b>Other comprehensive income/(expense) for the year</b>	<b>14.5</b>	(6.0)
<b>Total comprehensive income for the year</b>	<b>118.1</b>	91.3
Attributable to:		
Equity holders of the parent	<b>117.9</b>	91.2
Non-controlling interests	<b>0.2</b>	0.1
	<b>118.1</b>	91.3

# Consolidated balance sheet

At 31 December 2018

	Note	2018 £m	2017 £m
<b>Non-current assets</b>			
Goodwill	9	163.9	157.6
Other intangible assets	10	43.0	43.4
Property, plant and equipment	11	546.6	520.5
Investment in associate	24	4.1	–
Deferred tax assets	19	23.6	24.5
Trade and other receivables	13	1.4	1.0
		<b>782.6</b>	747.0
<b>Current assets</b>			
Inventories	12	13.9	16.4
Current tax assets		7.0	12.8
Trade and other receivables	13	146.3	140.4
Cash and bank balances	14	38.5	41.0
Assets held for sale	15	1.8	2.1
		<b>207.5</b>	212.7
<b>Total assets</b>		<b>990.1</b>	959.7
<b>Current liabilities</b>			
Trade and other payables	20	140.4	138.4
Current tax liabilities		26.6	29.2
Borrowings	16	2.3	1.4
Provisions	22	4.7	8.7
		<b>174.0</b>	177.7
<b>Net current assets</b>		<b>33.5</b>	35.0
<b>Non-current liabilities</b>			
Retirement benefit obligations	30	16.8	15.2
Deferred tax liabilities	19	60.9	57.2
Provisions	22	9.6	8.7
Other payables	20	2.2	3.4
		<b>89.5</b>	84.5
<b>Total liabilities</b>		<b>263.5</b>	262.2
<b>Net assets</b>		<b>726.6</b>	697.5
<b>Equity</b>			
Share capital	23	33.1	33.1
Share premium account		177.1	177.1
Own shares		(14.8)	(7.2)
Other reserves		141.4	141.0
Translation reserves		61.9	45.9
Retained earnings		327.2	307.1
<b>Equity attributable to equity holders of the parent</b>		<b>725.9</b>	697.0
Non-controlling interests		0.7	0.5
<b>Total equity</b>		<b>726.6</b>	697.5

The financial statements of Bodycote plc, registered number 519057, were approved by the Board of Directors and authorised for issue on 8 March 2019.

They were signed on its behalf by:

**S.C. Harris**  
Director

**D. Yates**  
Director

# Consolidated cash flow statement

For the year ended 31 December 2018

	Note	2018 £m	2017 £m
<b>Net cash from operating activities</b>	25	<b>173.3</b>	159.9
<b>Investing activities</b>			
Purchases of property, plant and equipment		(82.4)	(73.3)
Proceeds on disposal of property, plant and equipment and intangible assets		10.2	3.7
Purchases of intangible fixed assets		(1.8)	(5.2)
Acquisition of businesses		(8.3)	(14.2)
Disposal of businesses		0.7	–
<b>Net cash used in investing activities</b>		<b>(81.6)</b>	(89.0)
<b>Financing activities</b>			
Interest received		0.2	0.1
Interest paid		(1.9)	(2.1)
Dividends paid	7	(81.8)	(30.6)
Repayments of bank loans		(40.7)	(5.0)
Payments of obligations under finance leases		–	(0.1)
New bank loans raised		40.0	–
Own shares purchased/settlement of share options		(10.6)	–
<b>Net cash used in financing activities</b>		<b>(94.8)</b>	(37.7)
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(3.1)</b>	33.2
<b>Cash and cash equivalents at beginning of year</b>		<b>39.6</b>	6.2
Effect of foreign exchange rate changes		(0.3)	0.2
<b>Cash and cash equivalents at end of year</b>	25	<b>36.2</b>	39.6

# Consolidated statement of changes in equity

For the year ended 31 December 2018

	Share capital £m	Share premium account £m	Own shares £m	Other reserves £m	Translation reserves £m	Retained earnings £m	Equity attributable to equity holders of the parent £m	Non-controlling interests £m	Total equity £m
1 January 2017	33.1	177.1	(8.0)	133.9	57.5	234.3	627.9	0.4	628.3
Net profit for the year	–	–	–	–	–	97.1	97.1	0.2	97.3
Exchange differences on translation of overseas operations	–	–	–	–	(11.6)	–	(11.6)	(0.1)	(11.7)
Actuarial losses on defined benefit pension schemes net of deferred tax	–	–	–	–	–	5.7	5.7	–	5.7
<b>Total comprehensive income for the year</b>	–	–	–	–	(11.6)	102.8	91.2	0.1	91.3
Acquired in the year/settlement of share options	–	–	0.8	(0.7)	–	–	0.1	–	0.1
Share-based payments	–	–	–	7.8	–	–	7.8	–	7.8
Deferred tax on share-based payment transactions	–	–	–	–	–	0.6	0.6	–	0.6
Dividends paid	–	–	–	–	–	(30.6)	(30.6)	–	(30.6)
<b>31 December 2017</b>	<b>33.1</b>	<b>177.1</b>	<b>(7.2)</b>	<b>141.0</b>	<b>45.9</b>	<b>307.1</b>	<b>697.0</b>	<b>0.5</b>	<b>697.5</b>
Net profit for the year	–	–	–	–	–	103.2	103.2	0.4	103.6
Exchange differences on translation of overseas operations	–	–	–	–	16.0	–	16.0	(0.2)	15.8
Actuarial gains on defined benefit pension schemes net of deferred tax	–	–	–	–	–	(1.3)	(1.3)	–	(1.3)
<b>Total comprehensive income for the year</b>	–	–	–	–	16.0	101.9	117.9	0.2	118.1
Return of capital to shareholders and redemption of B shares	–	–	–	–	–	(0.2)	(0.2)	–	(0.2)
Acquired in the year/settlement of share options	–	–	(7.6)	(3.4)	–	0.4	(10.6)	–	(10.6)
Share-based payments	–	–	–	3.8	–	–	3.8	–	3.8
Deferred tax on share-based payment transactions	–	–	–	–	–	(0.2)	(0.2)	–	(0.2)
Dividends paid	–	–	–	–	–	(81.8)	(81.8)	–	(81.8)
<b>31 January 2018</b>	<b>33.1</b>	<b>177.1</b>	<b>(14.8)</b>	<b>141.4</b>	<b>61.9</b>	<b>327.2</b>	<b>725.9</b>	<b>0.7</b>	<b>726.6</b>

Included in other reserves is the capital redemption reserve of £129.8m (2017: £129.8m) and the share-based payments reserve of £10.8m (2017: £10.4m).

The own shares reserve represents the cost of shares in Bodycote plc purchased in the market. At 31 December 2018, 1,839,860 (2017: 1,171,190) ordinary shares of 17 3/11p each were held by the Bodycote International Employee Benefit Trust to satisfy share-based payments under the Group's incentive schemes (see note 27).

# Group accounting policies

## Year ended 31 December 2018

### Basis of accounting

The financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS). The financial statements have also been prepared in accordance with IFRS adopted by the European Union and therefore the Group financial statements comply with Article 4 of EU IAS Regulation as adopted for use in the EU.

The Group has adopted Standards and Interpretations issued by the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee of the IASB (IFRIC). Individual standards and interpretations have to be adopted by the European Commission (EC) and the process leads to a delay between the issue and adoption of new standards and in some cases amendment by the EC.

International Financial Reporting Standards are subject to ongoing amendment by the IASB and subsequent endorsement by the EC and are therefore subject to change.

The financial statements have been prepared on the historical cost basis, with the exception of accounting for certain financial instruments. Historical cost is generally based on the fair value of the consideration given up in exchange for the assets. The principal accounting policies adopted are set out below.

### Going concern

The directors have at the time of approving the financial statements a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis of accounting in preparing the financial statements. Further detail is contained in the Chief Financial Officer's report on page 26.

### Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. A subsidiary is an entity controlled, directly or indirectly, by Bodycote PLC. Control exists when the Group has power over the subsidiary, has exposure or rights to the variable returns from its involvement with a subsidiary and then holds ability to use its power to affect its returns.

The results of subsidiaries acquired or disposed during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used in line with those used by the Group. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Non-controlling interests in subsidiaries are identified separately from the Group's equity therein. Those interests of non-controlling shareholders that are present ownership interests entitling their holders to a proportionate share of net assets upon liquidation may initially be measured at fair value or at the non-controlling interests' proportionate share of the fair value of the acquiree's identifiable net assets.

The choice of measurement is made on an acquisition-by-acquisition basis. Other non-controlling interests are initially measured at fair value.

Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition plus the non-controlling interests' share of subsequent changes in equity. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Changes in the Group's interests in subsidiaries that do not result in a loss of control are accounted for as equity transactions. The carrying amount of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the Company.

When the Group loses control of a subsidiary, the profit or loss on disposal is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), less liabilities of the subsidiary and any non-controlling interests. Amounts previously recognised in other comprehensive income in relation to the subsidiary are accounted for (i.e. reclassified to profit or loss or transferred directly to retained earnings) in the same manner as would be required if the relevant assets or liabilities were disposed of. The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under IAS 39 Financial Instruments: Recognition and Measurement or, when applicable, the costs on initial recognition of an investment in an associate or jointly controlled entity.

### Key sources of estimation uncertainty

The key assumptions concerning the future, and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are discussed below.

### Taxation

The Group operates in a number of countries and is subject to taxes in numerous jurisdictions. Significant estimation is required in determining the provision for taxes based upon the interpretation of applicable tax legislation on a country-by-country basis and an assessment of the likely outcome of any open tax computations. Amounts provided are accrued based on management's interpretation of country-specific tax laws and the likelihood of settlement which may take several years to conclude. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences could have a consequent adverse impact on the Group's income statement in the period in which such determination is made. Please refer to note 6 on page 107 and note 30 on page 128 for further details.

# Group accounting policies continued

## Year ended 31 December 2018

Due to the uncertainty associated with such tax matters, on their conclusion the final outcome may vary significantly. Whilst a range of outcomes is reasonably possible, the extent of this range is difficult to define due to the nature of the risks, their inter-dependency and the numerous Tax Authorities involved. Tax provisions as at 31 December 2018 totalled £16.1m (2017: £17.5m).

### Retirement benefit schemes

Accounting for retirement benefit schemes under IAS 19 (revised) requires an assessment of the future benefits payable in accordance with actuarial assumptions. The discount rate applied in the calculation of scheme liabilities is a key source of estimation uncertainty for the Group. Details of the accounting policies applied in respect of retirement benefit schemes are set out on page 93 also refer to note 29 on page 123 for further details.

No other areas of key sources of estimation uncertainty have been identified, including those in relation to Brexit.

### Critical judgements in applying the Group's accounting policies

In the course of preparing the financial statements, no judgements have been made in the process of applying the Group's accounting policies, other than those involving estimations (above), that have had a significant effect on the amounts recognised in the financial statements.

### Investments in associates

An associate is an entity over which the Group is in a position to exercise significant influence, but not control or joint control, through participation in the financial and operating policy decisions of the investee.

The results and assets and liabilities of associates are incorporated in these financial statements using the equity method of accounting. Investments in associates are carried in the balance sheet at cost as adjusted by post-acquisition changes in the Group's share of the net assets of the associate, less any impairment in the value of individual investments. Losses of an associate in excess of the Group's interest in that associate (which includes any long-term interests that, in substance, form part of the Group's net investment in the associate) are recognised only to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

Any excess of the cost of acquisition over the Group's share of the fair values of the identifiable assets, liabilities and contingent liabilities of the associate at the date of acquisition is recognised as goodwill. The goodwill is included within the carrying amount of the investment. Any deficiency of the cost of acquisition below the Group's share of the fair values of the identifiable assets, liabilities and contingent liabilities of the associate at the date of acquisition (i.e. discount on acquisition) is credited in profit and loss in the period of acquisition.

Where a Group company transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate. Losses may provide evidence of an impairment of the asset transferred, in which case appropriate provision is made for impairment.

### Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

### Goodwill

Goodwill arising in a business combination is recognised as an asset at the date that control is acquired (the acquisition date). Goodwill is measured as the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of a subsidiary or associate at the date of acquisition. If after restatement, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

Goodwill is not amortised but is reviewed for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment at least annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to assets of the unit on a pro-rata basis. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary or associate, the attributable amount of goodwill is included in the determination of the profit or loss on disposal. Goodwill arising on acquisitions before the date of transition to IFRS has been retained at the previous UK GAAP amounts, subject to being tested for impairment at that date. Goodwill written off to reserves under UK GAAP prior to 1998 has not been reinstated and is not included in determining any subsequent profit or loss on disposal.

### Revenue recognition

The Group predominantly has one revenue stream relating to customer specific thermal processing services with either identifiable customer contracts or specific terms and conditions and pricing specific performance obligations. Revenue is recognised net of discounts, VAT and other sales-related taxes. In general, the services provided to the Group's customers contain one or more performance obligations. Revenue is recognised on completion of each of these performance obligations. The determination of the transaction price is based upon pricing as agreed with the customer. Revenue is recognised on completion of the services rendered.

Other operating income represents scrap sales, asset sales and other items of operating income not provided in the normal course of business.

## The Group as lessee

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are recognised as assets of the Group at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability.

Finance charges are charged directly against income.

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the lease term.

## Foreign currencies

Transactions in currencies other than pounds sterling are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Gains and losses arising on retranslation are included in net profit or loss for the period.

Exchange differences are recognised in profit or loss in the period in which they arise except for:

- exchange differences on transactions entered into to minimise certain foreign currency risks (see page 114); and
- exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur (therefore forming part of the net investment in the foreign operation) which are recognised initially in the consolidated statement of comprehensive income and reclassified from equity to profit or loss on disposal or partial disposal of the net investment.

On consolidation, the assets and liabilities of the Group's overseas operations are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation differences are recognised as income or as expenses in the period in which the operation is disposed of.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate. The Group has elected to treat goodwill and fair value adjustments arising on acquisitions before the date of transition to IFRS as sterling-denominated assets and liabilities.

## Borrowing costs

Borrowing costs are recognised in profit or loss in the period in which they are incurred. Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that take a substantial period of time to get ready for their intended use, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use.

## Operating profit

Operating profit is stated after charging restructuring costs, goodwill impairment, amortisation of acquired intangible assets and after the post-tax share of results of associates but before investment income and finance costs.

## Exceptional items

The Group considers exceptional items to be those which derive from events or transactions which are significant for separate disclosure by virtue of their size or incidence in order for the user to obtain a proper understanding of the Group's financial performance. These items include, but are not limited to, significant acquisition costs, impairment charges, significant reorganisation costs and profits and losses on disposal of subsidiaries and other one off items which meet this definition; this included the impact of the US Tax Reform in the prior year.

## Retirement benefit costs

Payments to defined contribution schemes are recognised as an expense when employees have rendered service entitling them to the contributions. Payments made to state-managed retirement benefit schemes are dealt with as payments to defined contribution schemes where the Group's obligations under the schemes are equivalent to those arising in a defined contribution retirement benefit scheme.

For defined benefit schemes, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out at the end of each reporting period. Remeasurement comprising actuarial gains and losses, the effect of the asset ceiling (if applicable) and the return on scheme assets (excluding interest) are recognised immediately in the balance sheet with a charge or credit to the statement of comprehensive income in the period in which they occur. Remeasurement recorded in the statement of comprehensive income is not recycled. Past service cost is recognised in profit or loss in the period of scheme amendment. Net interest is calculated by applying a discount rate to the defined benefit liability or asset. Defined benefit costs are split into three categories:

- current service cost, past-service cost and gains and losses on curtailments and settlements;
- net interest expense or income; and
- remeasurement.

The Group presents the first two components of defined benefit costs within cost of sales and administrative expenses (see note 3) in its consolidated income statement. Curtailment gains and losses are accounted for as past-service cost.

Net-interest expense or income is recognised within finance costs (see note 5).

# Group accounting policies continued

## Year ended 31 December 2018

The retirement benefit obligation recognised in the consolidated balance sheet represents the deficit or surplus in the Group's defined benefit schemes. Any surplus resulting from this calculation is limited to the present value of any economic benefits available in the form of refunds from the schemes or reductions in future contributions to the schemes.

A liability for a termination benefit is recognised at the earlier of when the entity can no longer withdraw the offer of the termination benefit and when the entity recognises any related restructuring costs.

### Taxation

The tax expense represents the sum of the tax currently payable and deferred tax.

The tax currently payable is based on taxable profit for the year or tax assessment adjustments made to prior years. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised based on tax laws and rates that have been enacted or substantively enacted at the balance sheet date. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited in other comprehensive income, in which case the deferred tax is also dealt with in other comprehensive income.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

### Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and any recognised impairment loss.

Depreciation is charged so as to write off the cost of assets, other than land and properties under construction, less their residual values, over their estimated useful lives, using the straight-line method, on the following bases:

Freehold buildings	2%
Leasehold property	over the period of the lease
Fixtures and fittings	10%–20%
Plant and machinery	5%–20%
Motor vehicles	20%–33%

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, over the term of the relevant lease. The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

Assets in the course of construction are carried at cost, plus appropriate borrowing costs, less any recognised impairment loss. Depreciation commences when the assets are ready for their intended use.

### Business combinations

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values (at the date of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit or loss as incurred.

Subsequent changes in such fair values are adjusted against the cost of acquisition where they qualify as measurement period adjustments. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are accounted for in accordance with relevant IFRSs.



The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 (2008) are recognised at their fair value at the acquisition date, except that:

- deferred tax assets or liabilities and liabilities or assets related to employee benefit arrangements are recognised and measured in accordance with IAS 12 Income Taxes and IAS 19 (revised) Employee Benefits respectively; and
- liabilities or equity instruments related to the replacement by the Group of an acquiree's share-based payment awards are measured in accordance with IFRS 2 Share-based Payment.

Assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations are measured in accordance with that standard.

### Intangible assets

Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortisation and accumulated impairment losses. Intangible assets under development are carried at cost (less any accumulated impairment losses) until available for use. Intangible assets acquired in a business combination and recognised separately from goodwill are initially recognised at fair value at the acquisition date (which is regarded as their cost). Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses.

Amortisation of these assets is recognised in the Consolidated Income Statement on a straight-line basis over their estimated useful lives, on the following basis:

Software	10%–33%
Non-compete agreements	20%–33%
Customer relationships	7%–10%

Amortisation is recognised within administration expenses.

### Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately.

### Inventories

Inventories are stated at the lower of cost and net realisable value and is accounted for on a first in, first out basis or, in some cases, a weighted-average basis, if deemed more appropriate for the business. For finished goods and work-in-progress, cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

### Financial instruments

Financial assets and financial liabilities are recognised on the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

### Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for trade receivables, which do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for expected credit losses and estimated irrecoverable amounts.

### Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and demand deposits and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

### Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

# Group accounting policies continued

## Year ended 31 December 2018

### Bank borrowings

Interest-bearing bank loans and overdrafts are recorded at the fair value, net of transaction costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accruals basis to the income statement using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

### Other financial liabilities

Other financial liabilities are not interest-bearing and are stated at their nominal value.

### Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

### Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

### Impairment of financial assets

Financial assets are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

Objective evidence of impairment could include:

- significant financial difficulty of the customer or counterparty; or
- default or delinquency in payments.

For certain categories of financial asset, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period, as well as observable changes in national or local economic conditions that correlate with default on receivables.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, where the carrying amount is reduced through the use of an allowance account. When a trade receivable is considered uncollectable, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

### Derivative financial instruments

The Group uses derivative financial instruments, in particular interest rate swaps, foreign currency swaps and forward exchange contracts, to manage the financial risks arising from the business activities and the financing of those activities. The Group does not use derivative financial instruments for speculative purposes.

The use of financial derivatives is governed by the Group's policies approved by the Board of Directors, which provide written principles on the use of financial derivatives.

Derivative financial instruments are initially recognised as assets and liabilities measured at their fair value on the balance sheet date. Changes in the fair value of any derivative instruments that do not fulfil the criteria for hedge accounting contained in IAS 39 Financial Instruments: Recognition and Measurement are recognised immediately in the income statement. A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months.

### Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, when it is probable that the Group will be required to settle that obligation and when a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation and the effect of the adjustment is material in relation to the financial statements, its carrying amount is the present value of those cash flows.

### Share-based payments

The Group has applied the requirements of IFRS 2 Share-based Payments.

The Group issues equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period. At each balance sheet date, the Group revises its estimate of the number of equity instruments expected to vest as a result of the effect of non-market based vesting conditions. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimates with a corresponding adjustment to the equity-settled employee benefits reserve.

## General information

Bodycote plc is a company incorporated in the United Kingdom under the Companies Act. The address of the registered office is given on page 39.

The nature of the Group's operations and its principal activities are included within the Group's Strategic report.

Information on the Group's objectives, policies and processes are included within the Group's Strategic report.

Items included in the financial statements of each entity in the Group are measured using the currency of the primary economic environment in which the entity operates. The consolidated financial statements are presented in pounds sterling, which is the functional and presentation currency of the Parent. Foreign operations are included in accordance with the policies set out in the Foreign Currencies accounting policy on page 93.

## Adoption of new and revised standards

In the current year, the following new and revised standards and interpretations have been adopted:

### ■ IFRS 9 Financial instruments

The standard was adopted on 1 January 2018, replacing IAS 39 Financial Instruments. This standard covers the classification, measurement, impairment and de-recognition of financial assets and financial liabilities together with a new hedge accounting model. IFRS 9 requires the group to recognise expected credit losses and to update these estimates periodically to reflect changes in the credit risk of financial assets. The Group transition to this standard has not had a material impact on the financial statements.

### ■ IFRS 15 Revenue from contracts with customers

The standard was adopted on 1 January 2018, replacing IAS 11 Construction Contracts and IAS 18 Revenue. This standard requires the separation of performance obligations within contracts with customers and the contractual value to be allocated to each of the performance obligations. Revenue is then recognised as each performance obligation is satisfied. Retrospective application in the comparative year ending 31 December 2017 is optional; however, the Group did not undertake this option. The Group transition to this standard has not had a material impact on the financial statements.

### ■ Clarifications to IFRS 15 Clarifications to IFRS 15 Revenue from contracts with customers

### ■ Amendments to IFRS 2 Classification and measurement of share-based payment transactions

### ■ IFRIC 22 Foreign currency transactions and advance consideration

The above interpretations and revised standards have not had any material impact on the amounts reported in these financial statements or the disclosures required. Other changes to standards and amendments issued but not yet effective are not expected to have a material impact on the Group's financial statements.

At the date of authorisation of these financial statements, the following standard and interpretation which has not been applied in these financial statements were in issue but not yet effective:

### ■ IFRS 16 Leases

IFRS 16, Leases, will be effective for accounting periods beginning on or after 1 January 2019 and will introduce changes to lessee accounting by removing the distinction between operating and finance leases, requiring the recognition of a right-of-use asset and a lease liability at the commencement of all leases. Leases previously classified as operating leases with lease payments recorded in the Consolidated Income Statement will now be included in the Consolidated Balance Sheet.

The Group has elected to apply the full retrospective implementation approach. Whilst the Group is party to approximately 1,300 leases, a large proportion of these are short-term in nature and not individually material in value. The Group has elected to apply a practical expedient which excludes lease agreements which are short-term in nature or low value from being recognised as leases according to IFRS 16. In addition the Group has also taken the option to 'grandfather' the assessment of which contracts are or contain leases.

IFRS 16 application will result in an increase in non-current assets and financial liabilities due to the recording of the right-of-use asset and future lease liabilities. Operating profit is expected to increase, although this increase is offset by higher interest expense resulting in an insignificant impact on net profit. EBITDA increases due to the replacement of the operating lease expense with amortisation of the leased assets.

The Group estimates the financial impact of adopting IFRS 16 on key metrics at 31 December 2018 to be an approximate:

- Increase in financial liabilities of £80m
- Increase in right-of-use assets of £74m
- Increase operating profit by £2m
- Increase in finance costs of £2m
- Earnings per share unchanged

# Notes to the consolidated financial statements

Year ended 31 December 2018

## 1. Alternative performance measures (APMs)

Bodycote uses various APMs, in addition to those reported under IFRS, as management believe these measures enable users of the financial statements to assess the underlying trading performance of the business. The APMs used include headline operating profit, return on sales, headline profit before taxation, EBITDA, headline EBITDA, headline tax rate, headline earnings per share (EPS), headline operating cash flow, free cash flow, headline operating cash conversion, net cash and return on capital employed (ROCE). These measures reflect the underlying trading performance of the business as they exclude certain non-operational items, acquisition costs and amortisation of acquired intangible assets. The Group also uses revenue growth percentages adjusted for the impact of foreign exchange movements, where appropriate, also to better represent the underlying performance of the business. The measures described above are also used in the targeting process for executive and management annual bonuses (headline operating profit, operating cash-flow) and share schemes (headline operating profit, headline operating cash flow, headline EPS).

The constant exchange rate comparison uses the current year reported segmental information, stated in the relevant functional currency, and translates the results into its presentational currency using the prior year's monthly exchange rates. Expansionary capital expenditure is defined as capital expenditure invested to grow the Group's business.

APMs are defined and reconciled to the IFRS statutory measure as follows:

### Headline operating profit

	2018 £m	2017 £m
Statutory operating profit	134.1	119.4
Add back:		
Amortisation of acquired intangibles	3.7	4.5
Acquisition costs	0.5	–
<b>Headline operating profit</b>	<b>138.3</b>	<b>123.9</b>

### Return on sales

	2018 £m	2017 £m
Headline operating profit	138.3	123.9
Revenue	728.6	690.2
<b>Return on sales</b>	<b>19.0%</b>	<b>18.0%</b>

### Headline profit before taxation

	2018 £m	2017 £m
Profit before taxation	132.2	117.0
Add back:		
Amortisation of acquired intangibles	3.7	4.5
Acquisition costs	0.5	–
<b>Headline profit before taxation</b>	<b>136.4</b>	<b>121.5</b>

### EBITDA and Headline EBITDA (Earnings Before Interest, Taxation, Depreciation, and Amortisation)

	2018 £m	2017 £m
Operating profit	134.1	119.4
Depreciation and amortisation	65.7	64.3
Impairment of fixed assets	1.8	0.4
Profit on disposal of property, plant and equipment	(1.7)	(0.7)
Loss on disposal of businesses	0.6	–
Share-based payments	3.8	7.8
<b>EBITDA</b>	<b>204.3</b>	<b>191.2</b>
Acquisition costs	0.5	–
<b>EBITDA and Headline EBITDA</b>	<b>204.3</b>	<b>191.2</b>

### Headline tax rate

	2018 £m	2017 £m
Headline tax charge	29.5	27.8
Headline profit before taxation	136.4	121.5
<b>Headline tax rate</b>	<b>21.7%</b>	<b>22.9%</b>

**Headline tax charge** excludes tax on amortisation of acquired intangibles and US tax reform impact in 2017: £0.9m (2017: £8.1m).

**Headline earnings per share** A detailed reconciliation is provided in note 8.

## 1. Alternative performance measures (APMs) continued

### Headline operating cash flow

	2018 £m	2017 £m
Cash generated by operations	197.8	182.8
Less:		
Net capital expenditure	(74.0)	(74.8)
Add:		
Restructuring cash flows	4.4	3.7
Acquisition costs	0.5	–
<b>Headline operating cash flow</b>	<b>128.7</b>	<b>111.7</b>

### Free cash flow

	2018 £m	2017 £m
Cash generated by operations	197.8	182.8
Less:		
Net capital expenditure	(74.0)	(74.8)
Financing costs	(1.9)	(2.1)
Taxation	(24.5)	(22.9)
<b>Free cash flow</b>	<b>97.4</b>	<b>83.0</b>

### Headline operating cash conversion

	2018 £m	2017 £m
Headline operating cashflow	128.7	111.7
Headline operating profit	138.3	123.9
<b>Headline operating cash conversion</b>	<b>93.0%</b>	<b>90.2%</b>

### Net cash

	2018 £m	2017 £m
Cash and bank balances	38.5	41.0
Bank overdrafts (included in borrowings)	(2.3)	(1.4)
<b>Net cash</b>	<b>36.2</b>	<b>39.6</b>

### Return on capital employed

	2018 £m	2017 £m
Headline operating profit	138.3	123.9
Average capital employed*	673.4	642.5
<b>Return on capital employed</b>	<b>20.5%</b>	<b>19.3%</b>

\* Capital employed is defined as net assets adjusted for net cash/(debt)

### Revenue and headline operating profit at constant exchange rates

Reconciled to revenue and headline operating profit in the table below:

	Year to 31 December 2018			
	ADE £m	AGI £m	Central cost and eliminations £m	Consolidated £m
Revenue	288.0	440.6	–	728.6
Constant exchange rates adjustment	4.0	3.7	–	7.7
<b>Revenue at constant exchange rates</b>	<b>292.0</b>	<b>444.3</b>	<b>–</b>	<b>736.3</b>
Headline operating profit	68.7	82.4	(12.8)	138.3
Constant exchange rates adjustment	1.0	0.4	–	1.4
<b>Headline operating profit at constant exchange rates</b>	<b>69.7</b>	<b>82.8</b>	<b>(12.8)</b>	<b>139.7</b>

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 2 Business and geographical segments

The Group has more than 180 facilities across the world serving a range of market sectors with various thermal processing services. The range and type of services offered is common to all market sectors.

In accordance with IFRS 8 Operating Segments, the segmentation of Group activity reflects the way the Group is managed by the chief operating decision-maker, being the Group Chief Executive, who regularly reviews the operating performance of six operating segments, split between the Aerospace, Defence & Energy (ADE) and Automotive & General Industrial (AGI) business areas, as follows:

- ADE – Western Europe;
- ADE – North America;
- ADE – Emerging markets;
- AGI – Western Europe;
- AGI – North America; and
- AGI – Emerging markets.

The split of operating segments by geography reflects the business reporting structure of the Group.

In accordance with the aggregation criteria of IFRS 8, the operating segments are aggregated into the Group's two key business areas, ADE and AGI, the split being driven by customer behaviour and requirements. Customers in the ADE segment tend to operate and purchase more globally and have long supply chains, whilst customers in the AGI segment tend to purchase more locally and have shorter supply chains.

Bodycote plants do not exclusively supply services to customers of a given market sector. Allocations of plants between ADE and AGI is therefore derived by reference to the preponderance of markets served.

Group	ADE	AGI	Central	Consolidated
	2018	2018	costs and	
	£m	£m	eliminations	2018
			2018	£m
<b>Revenue</b>				
Total revenue	<b>288.0</b>	<b>440.6</b>	–	<b>728.6</b>
<b>Result</b>				
Headline operating profit prior to share-based payments and unallocated central costs	<b>69.0</b>	<b>85.7</b>	–	<b>154.7</b>
Share-based payments (including social charges)	<b>(0.3)</b>	<b>(3.3)</b>	<b>(1.8)</b>	<b>(5.4)</b>
Unallocated central costs	–	–	<b>(11.0)</b>	<b>(11.0)</b>
Headline operating profit/(loss)	<b>68.7</b>	<b>82.4</b>	<b>(12.8)</b>	<b>138.3</b>
Amortisation of acquired intangible fixed assets	<b>(0.9)</b>	<b>(2.8)</b>	–	<b>(3.7)</b>
Acquisition costs	–	–	<b>(0.5)</b>	<b>(0.5)</b>
Segment result	<b>67.8</b>	<b>79.6</b>	<b>(13.3)</b>	<b>134.1</b>
Investment revenue				<b>0.2</b>
Finance costs				<b>(2.1)</b>
Profit before taxation				<b>132.2</b>
Taxation				<b>(28.6)</b>
Profit for the year				<b>103.6</b>

Inter-segment sales are not material in either year.

The Group does not rely on any individual major customers.

## 2 Business and geographical segments continued

	Western Europe 2018 £m	North America 2018 £m	Emerging markets 2018 £m	Total ADE 2018 £m
<b>Aerospace, Defence &amp; Energy</b>				
<b>Revenue</b>				
Total revenue	137.7	149.1	1.2	288.0
<b>Result</b>				
Headline operating profit/(loss) prior to share-based payments	33.6	35.9	(0.5)	69.0
Share-based payments (including social charges)	0.1	(0.4)	–	(0.3)
Headline operating profit/(loss)	33.7	35.5	(0.5)	68.7
Amortisation of acquired intangible fixed assets	0.2	(1.1)	–	(0.9)
Segment result	33.9	34.4	(0.5)	67.8
<b>Automotive &amp; General Industrial</b>				
<b>Revenue</b>				
Total revenue	272.0	106.5	62.1	440.6
<b>Result</b>				
Headline operating profit prior to share-based payments	57.9	11.8	16.0	85.7
Share-based payments (including social charges)	(2.5)	(0.6)	(0.2)	(3.3)
Headline operating profit	55.4	11.2	15.8	82.4
Amortisation of acquired intangible fixed assets	(0.3)	(2.5)	–	(2.8)
Segment result	55.1	8.7	15.8	79.6
<b>Group</b>				
	ADE 2017 £m	AGI 2017 £m	Central costs and eliminations 2017 £m	Consolidated 2017 £m
<b>Revenue</b>				
Total revenue	273.1	417.1	–	690.2
<b>Result</b>				
Headline operating profit prior to share-based payments and unallocated central costs	65.6	77.3	–	142.9
Share-based payments (including social charges)	(1.4)	(3.1)	(4.6)	(9.1)
Unallocated central costs	–	–	(9.9)	(9.9)
Headline operating profit/(loss)	64.2	74.2	(14.5)	123.9
Amortisation of acquired intangible fixed assets	(1.5)	(3.0)	–	(4.5)
Segment result	62.7	71.2	(14.5)	119.4
Investment revenue				0.1
Finance costs				(2.5)
Profit before taxation				117.0
Taxation				(19.7)
Profit for the year				97.3

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 2 Business and geographical segments continued

	Western Europe 2017 £m	North America 2017 £m	Emerging markets 2017 £m	Total ADE 2017 £m
<b>Aerospace, Defence &amp; Energy</b>				
<b>Revenue</b>				
Total revenue	126.0	145.7	1.4	273.1
<b>Result</b>				
Headline operating profit prior to share-based payments	30.7	34.7	0.2	65.6
Share-based payments (including social charges)	(0.5)	(0.9)	–	(1.4)
Headline operating profit	30.2	33.8	0.2	64.2
Amortisation of acquired intangible fixed assets	(0.3)	(1.2)	–	(1.5)
Segment result	29.9	32.6	0.2	62.7
<b>Automotive &amp; General Industrial</b>				
<b>Revenue</b>				
Total revenue	258.9	105.5	52.7	417.1
<b>Result</b>				
Headline operating profit prior to share-based payments	51.2	11.6	14.5	77.3
Share-based payments (including social charges)	(2.4)	(0.4)	(0.3)	(3.1)
Headline operating profit	48.8	11.2	14.2	74.2
Amortisation of acquired intangible fixed assets	(0.4)	(2.6)	–	(3.0)
Segment result	48.4	8.6	14.2	71.2
<b>Other information</b>				
	<b>ADE 2018 £m</b>	<b>AGI 2018 £m</b>	<b>Central costs and eliminations 2018 £m</b>	<b>Consolidated 2018 £m</b>
<b>Group</b>				
Gross capital additions	26.1	56.2	1.9	84.2
Depreciation and amortisation	23.6	40.1	2.0	65.7
<b>Balance sheet</b>				
Assets:				
Segment assets	366.2	557.8	66.1	990.1
Liabilities:				
Segment liabilities	(56.7)	(133.5)	(73.3)	(263.5)
	309.5	424.3	(7.2)	726.6
Allocation of head office net liabilities	(3.0)	(4.2)	7.2	–
Adjusted segment net assets	306.5	420.1	–	726.6



## 2 Business and geographical segments continued

	Western Europe 2018 £m	North America 2018 £m	Emerging markets 2018 £m	Total ADE 2018 £m
<b>Aerospace, Defence &amp; Energy</b>				
Gross capital additions	14.5	11.2	0.4	26.1
Depreciation and amortisation	10.3	13.1	0.2	23.6
<b>Balance sheet</b>				
Assets:				
Segment assets	175.4	185.9	4.9	366.2
Liabilities:				
Segment liabilities	(29.8)	(26.2)	(0.7)	(56.7)
Segment net assets	145.6	159.7	4.2	309.5
	Western Europe 2018 £m	North America 2018 £m	Emerging markets 2018 £m	Total AGI 2018 £m
<b>Automotive &amp; General Industrial</b>				
Gross capital additions	24.7	18.3	13.2	56.2
Depreciation and amortisation	23.6	10.7	5.8	40.1
<b>Balance sheet</b>				
Assets:				
Segment assets	285.4	178.1	94.3	557.8
Liabilities:				
Segment liabilities	(97.8)	(23.3)	(12.4)	(133.5)
Segment net assets	187.6	154.8	81.9	424.3
	ADE 2017 £m	AGI 2017 £m	Central costs and eliminations 2017 £m	Consolidated 2017 £m
<b>Group</b>				
Gross capital additions	33.6	39.7	5.2	78.5
Depreciation and amortisation	23.5	39.3	1.5	64.3
<b>Balance sheet</b>				
Assets:				
Segment assets	352.6	530.2	76.9	959.7
Liabilities:				
Segment liabilities	(60.2)	(133.2)	(68.8)	(262.2)
	292.4	397.0	8.1	697.5
Allocation of head office net assets	3.4	4.7	(8.1)	–
Adjusted segment net assets	295.8	401.7	–	697.5

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 2 Business and geographical segments continued

	Western Europe 2017 £m	North America 2017 £m	Emerging markets 2017 £m	Total ADE 2017 £m
<b>Aerospace, Defence &amp; Energy</b>				
Gross capital additions	23.4	9.3	0.9	33.6
Depreciation and amortisation	10.0	13.4	0.1	23.5
<b>Balance sheet</b>				
Assets:				
Segment assets	168.0	179.9	4.7	352.6
Liabilities:				
Segment liabilities	(30.8)	(28.4)	(1.0)	(60.2)
Segment net assets	137.2	151.5	3.7	292.4

	Western Europe 2017 £m	North America 2017 £m	Emerging markets 2017 £m	Total AGI 2017 £m
<b>Automotive &amp; General Industrial</b>				
Gross capital additions	20.1	12.6	7.0	39.7
Depreciation and amortisation	23.6	10.5	5.2	39.3
<b>Balance sheet</b>				
Assets:				
Segment assets	292.3	153.2	84.7	530.2
Liabilities:				
Segment liabilities	(96.7)	(20.6)	(15.9)	(133.2)
Segment net assets	195.6	132.6	68.8	397.0

### Geographical information

The Group's revenue from external customers and information about its segment assets (non-current assets excluding financial instruments, deferred tax assets and other financial assets) by country are detailed below:

	Revenue from external customers		Non-current assets	
	2018 £m	2017 £m	2018 £m	2017 £m
USA	243.6	236.8	298.2	272.1
France	111.3	111.9	75.3	78.1
Germany	101.0	91.4	84.2	86.5
UK	58.7	51.9	91.9	91.0
Sweden	44.4	38.9	34.8	36.8
Netherlands	29.6	29.4	22.8	22.7
Others	140.0	129.9	147.7	134.3
	<b>728.6</b>	690.2	<b>754.9</b>	721.5

### 3 Operating profit

	2018 £m	2017 £m
Revenue	728.6	690.2
Cost of sales	(451.0)	(429.9)
Gross profit	277.6	260.3
Other operating income	11.6	4.5
Distribution costs	(20.2)	(21.3)
Administration expenses	(128.4)	(118.6)
Other operating expenses	(2.3)	(1.0)
Headline operating profit	138.3	123.9
Amortisation of acquired intangible fixed assets	(3.7)	(4.5)
Acquisition costs	(0.5)	–
Operating profit	134.1	119.4

Profit for the year has been arrived at after charging/(crediting):

	2018 £m	2017 £m
Net foreign exchange gain	(0.1)	–
Inventory expensed	55.6	53.0
Depreciation of property, plant and equipment	60.1	58.1
Amortisation of intangible fixed assets	5.6	6.2
Gain on disposal of property, plant and equipment	(1.7)	(0.7)
Staff costs (see note 4)	291.1	283.8
Acquisition costs	0.5	–
Impairment (gain)/loss on trade receivables	(0.2)	0.8
Impairment of fixed assets – recognised in operating profit	1.8	0.4

The analysis of auditor's remuneration on a worldwide basis is as follows:

	2018 £m	2017 £m
Fees payable to the auditor for the audit of the annual accounts	0.2	0.1
Fees payable to the auditor and its associates for other services:		
The audit of the Group's subsidiaries	0.7	0.7
Total audit fees	0.9	0.8
Audit-related assurance services*	0.1	0.1
Total non-audit fees	0.1	0.1
	1.0	0.9

In addition to the amounts shown above, the auditor received fees of £7,700 (2017: £7,000) for the audit of the Group's pension schemes.

A description of the work of the Audit Committee is set out in the Audit Committee report and includes an explanation of how auditor objectivity and independence is safeguarded when non-audit services are provided by the auditor.

\* This includes £0.1m (2017: £0.1m) for the review of the half year report.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 4 Staff costs

The average monthly number of employees (including executive directors) was:

	<b>2018</b>	2017
	<b>Number</b>	Number
ADE:		
Western Europe	<b>921</b>	892
North America	<b>851</b>	827
Emerging markets	<b>21</b>	16
AGI:		
Western Europe	<b>2,021</b>	1,945
North America	<b>971</b>	962
Emerging markets	<b>748</b>	688
Shared services	<b>225</b>	235
Head office	<b>36</b>	29
	<b>5,794</b>	5,594
	<b>2018</b>	2017
	<b>£m</b>	£m
Their aggregate remuneration comprised:		
Wages and salaries	<b>247.6</b>	242.5
Social security costs	<b>34.6</b>	33.1
Other pension costs	<b>8.9</b>	8.2
	<b>291.1</b>	283.8

Included in wages and salaries are share-based payments resulting in a charge of £3.8m (2017: £78m).

Included in other pension costs are £7.0m relating to defined contribution schemes (2017: £6.7m), £1.9m relating to defined benefit schemes (2017: £1.5m) and £0.7m (2017: nil) relating to a one-off GMP equalisation charge as a result of the High Court ruling on 26 October 2018 in the landmark Lloyds Banking Group case on Guaranteed Minimum Pensions (GMPs).

Disclosure of individual directors' remuneration, share interests, share options, long term incentive schemes, pension contributions and pension entitlements required by the Companies Act 2006 and those specified for audit by the Listing Rules of the Financial Conduct Authority are shown in the tables in the Board report on remuneration on pages 56 to 77 and form part of these financial statements.

### 5 Finance costs

	<b>2018</b>	2017
	<b>£m</b>	£m
Interest on bank overdrafts and loans*	<b>0.1</b>	0.1
Net interest on the defined benefit pension liability	<b>0.2</b>	0.4
Other finance charges*	<b>1.8</b>	2.0
Total finance costs	<b>2.1</b>	2.5

\* Amounts arising on financial liabilities measured at amortised cost.

### 6 Taxation

	<b>2018</b>	2017
	<b>£m</b>	£m
Current taxation – charge for the year	<b>27.4</b>	28.1
Current taxation – adjustments in respect of previous years	<b>(0.4)</b>	(6.3)
Deferred tax (see note 19)	<b>1.6</b>	(2.1)
	<b>28.6</b>	19.7

The Group uses a weighted average country tax rate rather than the UK tax rate for the reconciliation of the charge for the year to the profit before taxation per the consolidated income statement. The Group operates in several jurisdictions, many of which have a tax rate in excess of the UK tax rate. As such, a weighted average country tax rate is believed to provide the most meaningful information to the users of the financial statements. The appropriate tax rate for this comparison is 26.5% (2017: 30.1%). The reduction in the weighted average country tax rate is mainly a result of the reduction in the US tax rate following the passing of the Tax Cuts and Jobs Act in December 2017.

## 6 Taxation continued

The charge for the year can be reconciled to the profit before taxation per the consolidated income statement as follows:

	<b>2018</b>	2017
	<b>£m</b>	£m
Profit before taxation	<b>132.2</b>	117.0
Tax at the weighted average country tax rate of 26.5% (2017: 30.1%)	<b>35.0</b>	35.2
Tax effect of expenses not deductible in determining taxable profit <sup>1</sup>	<b>0.6</b>	0.4
Impact of recognition or derecognition of deferred tax balances	<b>(0.9)</b>	(1.4)
Tax effect of other adjustments in respect of previous years:		
Current tax <sup>2</sup>	<b>(0.4)</b>	(7.0)
Deferred tax <sup>2</sup>	<b>0.2</b>	4.3
Effect of financing activities between jurisdictions <sup>3</sup>	<b>(7.9)</b>	(8.5)
Impact of trade and minimum corporate taxes	<b>1.5</b>	1.3
Impact of US Tax Cuts and Jobs Act treated as an exceptional item <sup>4</sup>	–	(6.4)
Effect of changes in statutory tax rates on deferred tax assets and liabilities	<b>(0.1)</b>	(0.1)
Other tax risk provision movements <sup>5</sup>	<b>0.6</b>	1.9
<b>Tax expense for the year</b>	<b>28.6</b>	19.7

Tax on items taken directly to equity is a credit of £0.7m (2017: £0.5m).

1. Those costs in various jurisdictions not deductible in calculating taxable profits.
2. 2018 prior year adjustments in current and deferred tax relate mainly to changes in assumptions and outcomes in UK and overseas tax positions, whilst the 2017 adjustments mainly related to changes in assumptions and outcomes in relation to overseas tax credits and other claims.
3. The Group is externally financed by a mix of cash flows from operations and short-term borrowings. Internally, operating subsidiaries are predominantly financed via intercompany loans. The effect is net of provisions based on management's estimation of tax risk relating to the potential disallowance of interest. £2.2m of interest deductions were restricted in the US in 2018 following the passing of the Tax Cuts and Jobs Act in December 2017.
4. Prior year net exceptional impact of the passing of the Tax Cuts and Jobs Act in the US in December 2017, made up of (i) £6.8m one-off tax gain resulting from a revaluation of the Group's US deferred tax liabilities, and (ii) £0.4m tax charge on accumulated overseas profits of US entities.
5. Includes provisions for local tax risks and non-financing cross border transactions.

As part of the calculation of the tax charge, the Group recognises a number of tax risk provisions in respect of ongoing tax enquiries and in recognition of the multinational tax environment that Bodycote operates in where the nature of the tax positions that are taken is often complex and subject to change. Tax provisions totalling £16.1m were recognised at 31 December 2018 (2017: £17.5m). The provisions included are based on an assessment of a range of possible outcomes to determine reasonable estimates of the consequences of tax authority audits in the various tax jurisdictions in which the Group operates. Management judgement is exercised to determine the quantum of the tax risk provisions based on an understanding of the appropriate local tax legislation, taking into consideration the differences of interpretation that can arise on a wide variety of issues including the nature of ongoing tax audits and the experience from earlier enquiries.

Note 30 to the accounts refers to a contingent liability in respect of the European Commission state aid investigation into the Group financing exemption in the UK controlled foreign company rules.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 7 Dividends

	2018 £m	2017 £m
Amounts recognised as distributions to equity holders in the year:		
Final dividend for the year ended 31 December 2017 of 12.1p (2016: 10.8p) per share	23.3	20.5
Special dividend for the year ended 31 December 2017 of 25.0p (2016: nil) per share	47.6	–
Interim dividend for the year ended 31 December 2018 of 5.7p (2017: 5.3p) per share	10.9	10.1
	<b>81.8</b>	30.6
Proposed final dividend for the year ended 31 December 2018 of 13.3p (2017: 12.1p) per share	25.2	23.0
Proposed special dividend for the year ended 31 December 2018 of 20.0p (2017: 25.0p) per share	38.3	47.9

The proposed final dividend is subject to approval by shareholders at the Annual General Meeting and have not been included as liabilities in these financial statements.

The dividends are waived on shares held by the Bodycote International Employee Benefit Trust.

### 8 Earnings per share

The calculation of the basic and diluted earnings per share is based on the following data:

	2018 £m	2017 £m
<b>Earnings</b>		
Earnings for the purpose of basic earnings per share being net profit attributable to equity holders of the parent	103.2	97.1
	<b>Number</b>	Number
<b>Number of shares</b>		
Weighted average number of ordinary shares for the purpose of basic earnings per share	190,289,981	190,250,855
Effect of dilutive potential ordinary shares:		
Share options	–	–
Weighted average number of ordinary shares for the purpose of diluted earnings per share	190,289,981	190,250,855
	<b>Pence</b>	Pence
<b>Earnings per share:</b>		
Basic	54.2	51.0
Diluted	54.2	51.0
	<b>£m</b>	£m
<b>Headline earnings</b>		
Net profit attributable to equity holders of the parent	103.2	97.1
Add back:		
Amortisation of acquired intangible fixed assets (net of tax)	2.8	2.9
Acquisition costs (net of tax)	0.5	–
Less:		
Impact of US Tax Cuts and Jobs Act treated as an exceptional item	–	(6.4)
<b>Headline earnings</b>	106.5	93.6
	<b>Pence</b>	Pence
<b>Headline earnings per share:</b>		
Basic	55.9	49.2
Diluted	55.9	49.2

## 9 Goodwill

	2018 £m	2017 £m
<b>Cost</b>		
At 1 January	218.8	222.5
Exchange differences	3.2	(4.1)
Recognised on acquisition of businesses	3.2	0.4
At 31 December	<b>225.2</b>	218.8
<b>Accumulated impairment</b>		
At 1 January	61.2	61.6
Exchange differences	0.1	(0.4)
At 31 December	<b>61.3</b>	61.2
<b>Carrying amount</b>	<b>163.9</b>	157.6

In 2017 a £0.4m hindsight adjustment was made in respect of a 2016 acquisition.

Goodwill acquired in a business combination is allocated, at acquisition, to the business units that are expected to benefit from that business combination. After recognition of impairment losses, the carrying amount of goodwill has been allocated to the Group's cash-generating units, which are summarised in the following operating segments:

	2018 £m	2017 £m
ADE:		
Western Europe	27.0	27.0
North America	48.4	47.5
AGI:		
Western Europe	24.3	24.1
North America	57.8	52.5
Emerging markets	6.4	6.5
	<b>163.9</b>	157.6

The Group tests goodwill at least annually for impairment, or more frequently if there are indications that goodwill might be impaired.

The recoverable amounts of the cash-generating units are determined from value in use calculations. The key assumptions for those calculations are the discount rates and growth rates in respect of future cash flows. Management estimates discount rates using pre-tax rates that reflect current market assessments of the time value of money and the risks specific to the cash-generating units. This rate is risk adjusted, for specific countries, where the Group perceives a risk premium is appropriate. The rates used to discount the forecast cash flows for cash-generating units are between 9.8% (2017: 11.7%) and 10.8% (2017: 12.7%). The recoverable amount is the sum of the discounted cash flows as forecasted for the coming five years, together with a further estimate of cash flows to perpetuity.

The forecast sales reflect management's expectation of how sales will develop at this point in the economic cycle. The expected profit margin reflects management's experience of each cash-generating unit's profitability at the forecast level of sales. As outlined in the Business review, these forecasts take into account the current and expected economic environment both in respect of geography and market sectors. Cash flows after five years are in the range of 2.3% (2017: 2.4%) to 5.4% (2017: 5.4%) depending on the geographical region of the cash-generating unit and are based on historical weighted average growth in GDP in the respective geographies. This rate does not exceed the average long-term growth rate for the relevant markets.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 9 Goodwill continued

If the goodwill allocated to a cash-generating unit represents more than 15% of the Group's total goodwill carrying value, the cash-generating unit is considered to be individually significant. The Group considers the North America ADE Heat Treatment and North America AGI Heat Treatment cash-generating units to be significant cash-generating units. The long-term growth rates applied to cash flows after five years and the rates used to discount the forecast cash flows for these significant cash-generating units are shown below:

	Goodwill carrying value	Long-term growth rate	Discount rate
	2018 £m	2018 %	2018 %
Cash generating unit			
North America ADE Heat Treatment	48.4	2.8	9.7
North America AGI Heat Treatment	57.8	2.8	9.7

	Goodwill carrying value	Long-term growth rate	Discount rate
	2017 £m	2017 %	2017 %
Cash generating unit			
North America ADE Heat Treatment	47.5	2.9	11.7
North America AGI Heat Treatment	52.5	2.9	11.7

The Group has conducted sensitivity analysis on the key assumptions applied to the value in use calculations for each cash generating unit. The separate sensitivity scenarios analysed include a reduction in the forecast sales of 20% in the first year of the forecast and reduction of the long-term revenue growth assumptions of 50% to 100% from year five of the cash flows.

The directors do not consider that there are any reasonable possible sensitivities for the business that could arise in the next 12 months that could result in a material impairment charge being recognised. The Board has concluded that no impairment charge is required in 2018.

### 10 Other intangible assets

	Software £m	Non- compete agreements £m	Customer relationships £m	Total £m
<b>Cost</b>				
At 1 January 2017	35.1	3.1	49.1	87.3
Exchange differences	(0.1)	–	(3.4)	(3.5)
Additions	5.2	–	–	5.2
Disposals	(0.3)	–	–	(0.3)
At 1 January 2018	<b>39.9</b>	<b>3.1</b>	<b>45.7</b>	<b>88.7</b>
Exchange differences	0.4	–	1.8	2.2
Additions	1.8	–	–	1.8
Acquired on acquisition of businesses (see note 24)	–	–	3.0	3.0
Disposals	(0.6)	–	–	(0.6)
Derecognised on disposal of businesses	(1.0)	–	–	(1.0)
<b>At 31 December 2018*</b>	<b>40.5</b>	<b>3.1</b>	<b>50.5</b>	<b>94.1</b>
<b>Amortisation</b>				
At 1 January 2017	15.3	3.0	23.2	41.5
Exchange differences	(0.1)	–	(2.0)	(2.1)
Charge for the year	1.7	0.1	4.4	6.2
Disposals	(0.3)	–	–	(0.3)
At 1 January 2018	<b>16.6</b>	<b>3.1</b>	<b>25.6</b>	<b>45.3</b>
Exchange differences	0.3	–	1.3	1.6
Charge for the year	1.9	–	3.7	5.6
Disposals	(0.6)	–	–	(0.6)
Derecognised on disposal of businesses	(0.8)	–	–	(0.8)
<b>At 31 December 2018</b>	<b>17.4</b>	<b>3.1</b>	<b>30.6</b>	<b>51.1</b>
<b>Carrying amount</b>				
<b>At 31 December 2018</b>	<b>23.1</b>	<b>–</b>	<b>19.9</b>	<b>43.0</b>
At 31 December 2017	23.3	–	20.1	43.4

Included in software assets are ongoing development costs related to the Group's ERP solutions. £9.1m (2017: £9.3m) of these costs are related to assets that are not yet available for use and are therefore not yet amortised. As such solutions become available for use they will be amortised according to Group policy.



## 11 Property, plant and equipment

	Land and buildings					Assets under construction £m	Total £m
	Freehold £m	Long leasehold £m	Short leasehold £m	Plant and machinery £m	Fixtures and fittings £m		
<b>Cost or valuation</b>							
At 1 January 2017	252.8	11.1	10.6	901.3	29.6	68.5	1,273.9
Additions	0.6	1.7	0.2	10.8	0.4	59.6	73.3
Acquisition of businesses	–	–	–	8.7	–	–	8.7
Exchange differences	(0.8)	0.1	(0.4)	(11.7)	0.2	(0.6)	(13.2)
Fair value adjustment	–	–	–	(0.6)	–	–	(0.6)
Transfer to assets held for sale	(1.4)	–	–	–	–	–	(1.4)
Recategorisation	6.1	(1.1)	3.1	51.7	1.1	(60.9)	–
Disposals	(3.9)	–	–	(31.2)	(1.5)	(0.1)	(36.7)
<b>At 1 January 2016</b>	<b>253.4</b>	<b>11.8</b>	<b>13.5</b>	<b>929.0</b>	<b>29.8</b>	<b>66.5</b>	<b>1,304.0</b>
Additions	0.6	0.1	0.3	8.5	0.4	72.5	82.4
Acquisition of businesses	–	–	–	2.1	–	–	2.1
Exchange differences	5.8	–	0.4	21.7	0.6	1.9	30.4
Transfer to assets held for sale	–	–	–	(0.8)	–	–	(0.8)
Recategorisation	7.4	0.2	3.2	53.7	1.3	(65.8)	–
Disposals	(9.3)	(1.6)	(0.9)	(39.3)	(2.0)	(0.1)	(53.2)
Disposal of businesses	(0.3)	–	–	(0.6)	(0.4)	–	(1.3)
<b>At 31 December 2018</b>	<b>257.6</b>	<b>10.5</b>	<b>16.5</b>	<b>974.3</b>	<b>29.7</b>	<b>75.0</b>	<b>1,363.6</b>
<b>Accumulated depreciation and impairment</b>							
At 1 January 2017	110.8	4.9	7.1	618.5	23.6	–	764.9
Charge for the year	6.5	1.0	0.7	48.4	1.5	–	58.1
Impairment losses incurred	–	–	–	0.4	–	–	0.4
Exchange differences	0.4	–	(0.1)	(5.5)	0.1	–	(5.1)
Transfer to assets held for sale	(0.6)	–	–	–	–	–	(0.6)
Recategorisation	1.1	(0.9)	–	(0.2)	–	–	–
Eliminated on disposals	(3.2)	–	–	(29.5)	(1.5)	–	(34.2)
<b>At 1 January 2018</b>	<b>115.0</b>	<b>5.0</b>	<b>7.7</b>	<b>632.1</b>	<b>23.7</b>	<b>–</b>	<b>783.5</b>
Charge for the year	6.5	1.1	0.9	50.2	1.4	–	60.1
Impairment losses incurred	–	–	0.1	1.7	–	–	1.8
Exchange differences	2.6	–	0.2	15.1	0.4	–	18.3
Transfer to assets held for sale	–	–	–	(0.5)	–	–	(0.5)
Recategorisation	(0.1)	0.1	–	(0.1)	0.1	–	–
Eliminated on disposals	(4.3)	(1.6)	(1.0)	(36.6)	(1.9)	–	(45.4)
Eliminated on disposal of businesses	(0.1)	–	–	(0.4)	(0.3)	–	(0.8)
<b>At 31 December 2018</b>	<b>119.6</b>	<b>4.6</b>	<b>7.9</b>	<b>661.5</b>	<b>23.4</b>	<b>–</b>	<b>817.0</b>
<b>Carrying amount</b>							
<b>At 31 December 2018</b>	<b>138.0</b>	<b>5.9</b>	<b>8.6</b>	<b>312.8</b>	<b>6.3</b>	<b>75.0</b>	<b>546.6</b>
At 31 December 2017	138.4	6.8	5.8	296.9	6.1	66.5	520.5

At 31 December 2018 the Group had entered into contractual commitments for the acquisition of property, plant and equipment amounting to £3.1m (2017: £2.6m).

In addition to the above, property, plant and equipment amounting to £1.8m (2017: £2.1m) has been classified as held for sale and is disclosed within current assets.

During the prior year a £0.6m fair value adjustment was made to the value of acquired plant and machinery from 2016.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 11 Property, plant and equipment continued

The Group restructured various operations during the year and identified £1.8m (2017: £0.4m) of asset impairments. Asset impairments broken down by business segment are as follows:

	<b>2018</b>	2017
	<b>£m</b>	£m
ADE:		
Western Europe	<b>0.1</b>	0.2
North America	<b>0.7</b>	–
AGI:		
Western Europe	<b>0.7</b>	0.2
North America	<b>0.3</b>	–
	<b>1.8</b>	0.4

It is the directors' view that there are no material differences between the value of the land owned and their carrying value in the balance sheet.

### 12 Inventories

	<b>2018</b>	2017
	<b>£m</b>	£m
Raw materials	<b>12.4</b>	13.2
Work-in-progress	<b>1.1</b>	2.9
Finished goods and goods for resale	<b>0.4</b>	0.3
	<b>13.9</b>	16.4

### 13 Trade and other receivables

	<b>2018</b>	2017
	<b>£m</b>	£m
<b>Amounts falling due within one year:</b>		
Amounts receivable for the supply of services	<b>120.1</b>	114.2
Other receivables	<b>17.2</b>	16.8
Prepayments	<b>9.0</b>	9.4
	<b>146.3</b>	140.4
<b>Amounts falling due after more than one year:</b>		
Other receivables and prepayments	<b>1.4</b>	1.0

The average credit period given to customers for the supply of services as at 31 December 2018 is 64 days (2017: 63 days). An allowance has been made for estimated irrecoverable amounts from the supply of services of £5.1m (2017: £5.5m). This allowance has been determined by reference to expected credit losses.

The carrying amount of trade and other receivables approximates their fair value.

Included in the Group's trade receivables balance are debtors with a carrying amount of £32.0m (2017: £29.2m) which are past due at the reporting date for which the Group has not provided as there has not been a significant change in credit quality and the amounts are still considered recoverable. The Group does not hold any collateral over these balances.

The average credit terms offered to customers is 36 days, with a range from 15 days to 68 days.

Ageing of past due but not impaired receivables:

	<b>2018</b>	2017
	<b>£m</b>	£m
31–60 days	<b>15.1</b>	13.9
61–90 days	<b>11.1</b>	11.1
91–120 days	<b>4.1</b>	2.1
Greater than 120 days	<b>1.7</b>	2.1
	<b>32.0</b>	29.2

### 13 Trade and other receivables continued

Movement in the allowance for doubtful debts:

	2018 £m	2017 £m
At 1 January	5.5	7.1
Impairment losses recognised	1.6	1.8
Amounts written off as uncollectable	(0.3)	(2.4)
Impairment losses reversed	(1.8)	(1.0)
Exchange differences	0.1	–
<b>At 31 December</b>	<b>5.1</b>	<b>5.5</b>

In determining the recoverability of a trade receivable the Group considers any change in the quality of the trade receivable from the date credit was initially granted up to the reporting date. The concentration of credit risk is limited due to the customer base being large and unrelated. Accordingly the directors believe that there is no further credit provision required in excess of the allowance for doubtful debts.

Included in the allowance for doubtful debts are individually impaired trade receivables with a gross balance of £6.2m (2017: £6.6m). The impairment recognised represents the difference between the carrying amount of these trade receivables and the present value of the expected proceeds. The Group does not hold any collateral over these balances.

Ageing of impaired trade receivables:

	2018 £m	2017 £m
Less than 3 months	0.1	1.5
3-12 months	3.8	3.7
Over 12 months	2.3	1.4
	<b>6.2</b>	<b>6.6</b>

### 14 Cash and bank balances

Cash and bank balances comprise cash held by the Group and short-term bank deposits with an original maturity of three months or less. The carrying amount of these assets approximates to their fair value. A breakdown of significant cash and bank balances by currency is as follows:

	2018 £m	2017 £m
Sterling	14.9	24.5
Euro	7.8	6.0
US Dollar	7.0	5.8
Mexican Peso	2.8	1.0
Swedish Krona	2.0	1.5
Other	4.0	2.2
<b>Total cash and bank balances</b>	<b>38.5</b>	<b>41.0</b>

### 15 Assets held for sale

Included in Property, plant and equipment is £1.8m (2017: £2.1m) of assets held for sale which consist exclusively of land and buildings currently not in use by the Group. It is expected that the disposal of these assets will be completed during 2019. The assets held for sale are analysed between operating segments as follows:

	2018 £m	2017 £m
ADE:		
North America	0.9	0.8
AGI:		
Western Europe	–	0.4
North America	0.9	0.9
	<b>1.8</b>	<b>2.1</b>

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 16 Borrowings

	<b>2018</b>	2017
	<b>£m</b>	£m
Bank overdrafts	<b>2.3</b>	1.4
Weighted average interest rate paid	<b>1.3%</b>	1.9%
Analysis of bank overdrafts by currency:		
US Dollar	<b>2.2</b>	0.6
Euro	–	0.6
Other	<b>0.1</b>	0.2
	<b>2.3</b>	1.4

Bank overdrafts are repayable on demand. No overdrafts are secured.

The Group holds a Revolving Credit Facility in the amount of £230m. This unsecured facility commenced on 3 April 2017 and matures on 3 April 2022. The multi-currency drawings under this facility carry an interest rate of between 0.90% and 1.75% above LIBOR. The applicable margin at 31 December 2018 was 0.90% (2017: 0.90%).

At 31 December 2018, the Group's principal borrowing facility had drawings of £nil (2017: £nil).

All borrowings are classified as financial liabilities measured at amortised cost. Given their short-term nature, the carrying amounts of bank overdrafts approximate their fair value.

## 17 Derivative financial instruments

The Group uses foreign currency forward contracts in the management of its exchange rate exposures. The contracts are primarily denominated in the currencies of the Group's principal markets. The unrecognised gains and losses were not material in either 2018 or 2017.

The following summarises the aggregate notional amount (aggregate face value) of all open contracts and their related fair values as of the balance sheet date:

	<b>Contractual or notional amount</b>	<b>Fair value</b>	Contractual or notional amount	Fair value
<b>Fair value hedges</b>				
Currency forward foreign exchange contracts	<b>0.9</b>	–	3.0	–

In accordance with IFRS 7 Financial Instruments: Disclosures, the Group's financial instruments are considered to be classified as level 2 instruments. Fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Fair value is determined using quoted forward exchange rates and yield curves derived from quoted interest rates matching maturities of the contracts.

The Group's interest rate risk is primarily in relation to its fixed rate borrowings (fair value risk) and floating rate borrowings (cash flow risk). From time to time the Group will use interest rate derivative contracts to manage its exposure to interest rate movements within Group policy. However, at the balance sheet date, the Group had no interest rate derivative contracts (2017: nil).

All forward foreign exchange contracts are on demand or due within one year.

## 18 Financial risk management

The Group's multinational operations expose it to a variety of financial risks. In the course of its business, the Group is exposed to foreign currency risk, interest rate risk, liquidity risk and credit risk. Financial risk management policies are set by the Board. The Group's treasury function provides a centralised service to the Group for funding, foreign exchange, interest rate management and counterparty risk. Treasury activities have the objective of minimising risk and treasury operations are conducted within a framework of policies and guidelines reviewed and authorised by the Board.

In accordance with its treasury policy, the Group does not use or hold derivative financial instruments for trading or speculative purposes. The Group may however use derivative instruments, for risk management purposes only, by specialist treasury personnel. The use of financial instruments, including derivatives, is permitted when approved by the Board, where the effect is to minimise risk for the Group. There has been no significant change during the financial year, or since the end of the year, to the types or scope of financial risks faced by the Group.

### Liquidity risk

Liquidity risk is defined as the risk that the Group might not be able to settle or meet its obligations on time or at a reasonable price. Liquidity risk arises as a result of mismatches between cash inflows and outflows from the business. This risk is monitored on a centralised basis through regular cash flow forecasting, a three-year rolling strategic plan, an annual budget agreed by the Board each December and a quarterly re-forecast undertaken during the financial year. To mitigate the risk, the resulting forecast net debt/cash is measured against the liquidity headroom policy which, at the current net debt/cash levels, requires committed facilities (plus long term loans in excess of one year) to exceed net debt by 50% (minimum facilities of £75m).

As at 31 December 2018, the Group had a revolving credit committed borrowing facility of £230.0m (2017: £230.0m) which, together with net cash of £36.2m (2017: £39.6m), resulted in available funds of £266.2m (2017: £269.6m). The Group also uses uncommitted short-term bank facilities to manage short-term liquidity but these facilities are excluded from the liquidity headroom policy. The Group manages longer-term liquidity through its committed bank facilities and will, if appropriate, raise funds on capital markets.

As at 31 December 2018 the Group's principal committed bank facility of £230.0m had a maturity date of 3 April 2022 (3.3 years to maturity) and had drawings of £nil (2017: £nil).

Cash management pooling, netting and concentration techniques are used to minimise borrowings. As at 31 December 2018, the Group had gross cash of £38.5m (2017: £41.0m).

### Credit risk

Credit risk primarily arises because a counterparty may fail to perform its obligations. The Group is exposed to credit risk on financial assets such as cash balances, derivative financial instruments and trade and other receivables.

The Group's credit risk is primarily attributable to its trade receivables. The amounts presented in the balance sheet are net of appropriate allowances for doubtful receivables. An allowance for impairment is made where there is an identified loss event which, based on previous experience, is evidence of a reduction in the recoverability of cash flows. The quantitative analysis of credit risk relating to receivables is included in note 13.

The credit risk on liquid funds and derivative financial instruments is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies.

The Group has no significant concentration of credit risk, with exposure spread over a large number of counterparties and customers. Further disclosure of the Group's financial instrument risk management activities is set out in note 17.

### Interest rate risk

Interest rate risk arises on borrowings and cash balances (and derivative liabilities and assets) which are at floating interest rates. Changes in interest rates could have the effect of either increasing or decreasing the Group's net profit. Under the Group's interest rate management policy, the interest rates on each of the Group's major currency monetary assets and liabilities are managed to achieve the desired mix of fixed and variable rates for each major net currency exposure. The major interest rate risk is to UK rates but exposures also exist to rates in the USA, Europe and Sweden. Measurement of this interest rate risk and its potential volatility to the Group's reported financial performance is undertaken on a monthly basis and the Board uses this information to determine, from time to time, an appropriate mix of fixed and floating rates.

As at 31 December 2018, 0% of gross debt and 0% of gross cash were at fixed rates (2017: 0% of gross debt, 0% of gross cash).

### Currency risk

Bodycote has operations in 23 countries and is therefore exposed to foreign exchange translation risk when the profits and net assets of these entities are consolidated into the Group accounts.

Ninety-two per cent of the Group's sales are in currencies other than sterling (including EUR 39%, USD 34% and SEK 6%). Cumulatively over the year, sterling rates moved such that the sales for the year were £7.7m lower than if sales had been translated at the rates prevailing in 2017.

It is Group policy not to hedge exposure for the translation of reported profits.

The Group's balance sheet translation policy is not to actively hedge currency net assets. However, where appropriate, the Group will still match centrally held currency borrowings to the net assets. The Group principally borrows in sterling but also maintains debt in US dollars, euro and Swedish krona, consistent with the location of the Group's assets. The Group recognises foreign exchange movements in equity for the translation of net investment hedging instruments and balances.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 18 Financial risk management continued

Transactional foreign exchange exposures arise when entities within the Group enter into contracts to pay or receive funds in a currency different from the functional currency of the entity concerned. It has been Group policy to hedge exposure to cash transactions in foreign currencies when a commitment arises, usually through the use of foreign exchange forward contracts. Even though approximately 92% of the Group's sales are generated outside the UK, the nature of the business is such that cross border sales and purchases are limited and immaterial for the Group.

#### Market risk sensitivity analysis

To represent management's best estimate of a reasonable range of potential outcomes, the Group has measured the estimated charge to the income statement and equity of either an instantaneous increase or decrease of 1% (100 basis points) in market interest rates or a 10% strengthening or weakening in sterling against all other currencies from the applicable rates as at 31 December 2018, for all financial instruments with all other variables remaining constant. This analysis is for illustrative purposes only. The sensitivity analysis excludes the impact of market risks on net post employment benefit obligations.

#### Interest rate sensitivity

The interest rate sensitivity analysis is based on the following assumptions:

- changes in market interest rates affect the interest income or expense of variable interest financial instruments;
- changes in market interest rates only affect the income statement in relation to financial instruments with fixed interest if these are recognised at their fair value; and
- changes in market interest rates affect the fair value of derivative financial instruments designated as hedging instruments.

Under these assumptions, a one percentage point fall or rise in market interest rates for all currencies in which the Group has variable net cash or net borrowings at 31 December 2018 would reduce or increase profit before tax by approximately £0.3m (2017: £0.4m increase). There is no significant impact on equity in the current or previous year.

#### Currency sensitivity

Taking the 2018 sales by currency, a 10% weakening/strengthening in the 2018 cumulative average rates for all currencies versus sterling would have given rise to a +£74.4m/-£66.2m movement in sales respectively. The impact on headline operating profit is affected by the mix of losses and profits in the various currencies. However, taking the 2018 operating profit mix, a 10% weakening/strengthening in 2018 cumulative average rates for all currencies would have given rise to a +£15.7m/-£12.6m movement in headline operating profit.

#### Counterparty risk

Counterparty risk encompasses settlement risk on derivative financial instruments and money market contracts and credit risk on cash, time deposits and money market funds. The Group monitors its credit exposure to its counterparties via their credit ratings (where applicable) and through its policy, thereby limiting its exposure to any one party to ensure there is no significant concentration of credit risk. Group policy is to enter into such transactions only with counterparties with a long-term credit rating of A-/A3 or better. However, acquired businesses occasionally have dealings with banks with lower credit ratings. Business with such banks is moved as soon as practicable.

## 19 Deferred tax

The following are the major deferred tax liabilities and (assets) recognised by the Group and movements thereon during the current and prior reporting periods:

	Accelerated tax depreciation £m	Tax losses £m	Retirement benefit obligations £m	Other £m	Total £m
At 1 January 2017	58.8	(3.2)	(5.3)	(14.0)	36.3
(Credit)/charge to income	1.6	1.3	(0.1)	2.0	4.8
Credit to equity	–	–	1.1	(0.5)	0.6
Acquisition of businesses	(0.4)	–	–	(0.3)	(0.7)
Transfers	(0.2)	–	0.1	0.1	–
Exchange differences	(1.8)	–	(0.2)	0.7	(1.3)
Effect of change in tax rate:					
Income statement <sup>1</sup>	(11.2)	(0.1)	–	4.4	(6.9)
Equity	–	–	(0.1)	–	(0.1)
<b>At 1 January 2018</b>	<b>46.8</b>	<b>(2.0)</b>	<b>(4.5)</b>	<b>(7.6)</b>	<b>32.7</b>
Charge/(credit) to income	<b>2.6</b>	<b>(0.5)</b>	<b>(0.6)</b>	<b>0.2</b>	<b>1.7</b>
Credit to equity	–	–	<b>0.5</b>	<b>0.2</b>	<b>0.7</b>
Acquisition of businesses	–	–	–	<b>0.9</b>	<b>0.9</b>
Disposal of businesses	–	–	<b>0.2</b>	–	<b>0.2</b>
Transfers	<b>(0.2)</b>	–	<b>0.1</b>	<b>0.1</b>	–
Exchange differences	<b>1.6</b>	–	<b>(0.1)</b>	<b>(0.3)</b>	<b>1.2</b>
Effect of change in tax rate:					
Income statement	<b>(0.1)</b>	–	–	–	<b>(0.1)</b>
<b>At 31 December 2018</b>	<b>50.7</b>	<b>(2.5)</b>	<b>(4.4)</b>	<b>(6.5)</b>	<b>37.3</b>

1. Prior year net impact of (i) £6.8m net one-off tax gain resulting from a revaluation of the Group's US deferred tax liabilities. This is in relation to the passing of the Tax Cuts and Jobs Act in the US in December 2017 that reduced the US Federal corporate income tax rate, (ii) £0.1m in relation to other tax rate change impacts.

The following is the analysis of the deferred tax balances for financial reporting purposes:

	2018 £m	2017 £m
Deferred tax liabilities	<b>60.9</b>	57.2
Deferred tax assets	<b>(23.6)</b>	(24.5)
	<b>37.3</b>	32.7

Other deferred tax assets relate to provisions recognised in the financial statements that are not yet deductible for tax purposes, in particular in relation to restructuring charges, share-based payments and local profit differences that are expected to reverse over time.

At the balance sheet date, the Group has unused tax losses of £34.2m (2017: £35.6m) available for offset against future profits. A deferred tax asset has been recognised in respect of £9.0m (2017: £7.3m) of such losses, based on management forecasts of future taxable profits against which the assets can be recovered in the relevant jurisdictions. No deferred tax asset has been recognised in respect of the remaining £25.2m (2017: £28.3m) of such losses where there remains uncertainty over the timing of utilisation relating to future profitability. The majority of losses may be carried forward indefinitely.

A deferred tax liability of £0.5m (2017: £0.5m) relating to the temporary differences on unremitted earnings of overseas subsidiaries has been recognised as the Group believes it is probable that these temporary differences will reverse in the foreseeable future. Temporary differences arising in connection with interests in associates and joint ventures are insignificant.

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 20 Trade and other payables

	2018 £m	2017 £m
<b>Amounts falling due within one year:</b>		
Trade payables	37.6	38.2
Other taxes and social security	24.8	23.5
Other payables	11.4	14.6
Accruals*	66.6	62.1
	<b>140.4</b>	<b>138.4</b>
<b>Amounts falling due after more than one year:</b>		
Other payables	2.2	3.4

\*Accruals include £31.1m (2017: £32.6m) of payroll-related accruals.

Trade payables and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade purchases as at 31 December 2018 is 36 days (2017: 40 days).

The directors consider that the carrying amount of trade payables approximates to their fair value.

## 21 Other financial liabilities

The following table details the Group's remaining contractual maturity for its financial liabilities. The table has been drawn up based on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay. The table includes both interest and principal cash flows.

	Less than 1 year 2018 £m	1-2 years 2018 £m	2-5 years 2018 £m	5+ years 2018 £m	Total 2018 £m
Non-interest bearing	83.7	2.9	3.6	5.3	95.5
Bank loans and overdrafts	2.3	–	–	–	2.3
Derivative financial instruments	0.9	–	–	–	0.9
	<b>86.9</b>	<b>2.9</b>	<b>3.6</b>	<b>5.3</b>	<b>98.7</b>
	Less than 1 year 2017 £m	1-2 years 2017 £m	2-5 years 2017 £m	5+ years 2017 £m	Total 2017 £m
Non-interest bearing	85.5	3.8	3.3	5.0	97.6
Bank loans and overdrafts	1.4	–	–	–	1.4
Derivative financial instruments	3.0	–	–	–	3.0
	89.9	3.8	3.3	5.0	102.0

We have reclassified certain prior-year amounts to conform to the current-year's presentation.

Of the £2.3m (2017: £1.4m) bank loans and overdrafts outflows disclosed above, £nil (2017: £nil) of bank loans are drawn under the committed facility maturing on 3 April 2022. The overdrafts are on demand and some are part of pooling arrangements, which include offsetting cash balances. Of the £0.9m (2017: £3.0m) derivative financial instruments outflows disclosed above, £0.9m (2017: £3.0m) are matched by derivative cash inflows, therefore the net impact on the balance sheet is £nil (2017: £nil).



## 22 Provisions

	Restructuring £m	Restructuring environmental £m	Environmental £m	Total £m
At 1 January 2018	4.1	4.7	8.6	17.4
Increase in provision	2.0	–	0.6	2.6
Release of provision	(0.9)	–	(0.5)	(1.4)
Utilisation of provision	(2.7)	(1.7)	(0.5)	(4.9)
Exchange difference	(0.1)	0.2	0.5	0.6
<b>At 31 December 2018</b>	<b>2.4</b>	<b>3.2</b>	<b>8.7</b>	<b>14.3</b>
Included in current liabilities				4.7
Included in non-current liabilities				9.6
				<b>14.3</b>

The restructuring provision materially relates to the costs associated with the closure of a number of Heat Treatment facilities over the last few years.

The Group provides for the costs of environmental remediation that have been identified, either as part of acquisition due diligence, or in other circumstances where remediation by the Group is required. This provision is reviewed annually and is separated into restructuring environmental and environmental to identify separately environmental provisions relating to the restructuring programme from those arising in the ordinary course of business.

The majority of cash outflows in respect of these liabilities are expected to occur within five years.

Whilst the Group's use of chlorinated solvents and other hazardous chemicals continues to reduce, the Group remains exposed to contingent liabilities in respect of environmental remediation liabilities. In particular, the Group could be subjected to regulatory or legislative requirements to remediate sites in the future. However, it is not possible at this time to determine whether and to what extent any liabilities exist, other than for those recognised above. Therefore no provision is recognised in relation to these items.

## 23 Share capital

	2018 £m	2017 £m
<b>Issued and fully paid:</b>		
191,456,172 (2017: 191,456,172) ordinary shares of 17 3/11p each	<b>33.1</b>	33.1

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 24 Acquisition and disposal of businesses

### Acquisition of businesses

On 4 October 2018, Bodycote acquired a facility in the US to strengthen the Group's network and to enhance the process offering in the USA. The acquisition fits well with the Group's automotive and general industrial strategy. This is the only acquisition during 2018.

The transaction has been accounted for by the purchase method of accounting and is summarised below:

	<b>2018</b>
	<b>£m</b>
<b>Fair value of net assets acquired:</b>	
Intangible fixed assets	<b>3.0</b>
Property, plant and equipment	<b>2.1</b>
Trade and other receivables	<b>0.7</b>
Trade and other payables	<b>(0.6)</b>
Cash and cash equivalents	<b>0.1</b>
Deferred tax liabilities	<b>(0.9)</b>
Bank loans	<b>(0.6)</b>
	<b>3.8</b>
Goodwill	<b>3.2</b>
<b>Total consideration</b>	<b>7.0</b>
Satisfied by:	
Cash consideration	<b>6.9</b>
Accrued consideration	<b>0.1</b>
<b>Net cash outflow arising on acquisition:</b>	
Cash consideration	<b>7.0</b>
Less: cash and cash equivalents acquired	<b>(0.1)</b>
	<b>6.9</b>

Acquisition-related costs amounted to £0.5m (2017: £nil).

The acquired business contributed £1.2m revenue and £0.3m headline operating profit for the period between the dates of acquisition and the balance sheet date.

If the acquisitions had been completed on the first day of the financial year, Group revenue would have been £732.8m and Group headline operating profit attributable to equity holders of the parent, stated prior to Group management charges, would have been £139.3m.

### Deferred payments on acquisitions

Payments totaling £1.4m were made during the year in respect of deferred consideration due on acquisitions made in 2016. The amounts were recorded in other receivables at 31st December 2017.

### Disposal of businesses

On 19 October Bodycote sold its shareholding in FHK GmbH (Steinbach) for consideration of £0.5m. During the year, the Steinbach facility contributed £1.0m (2017: £1.2m) to Group revenue and contributed headline operating profit/(loss) of £0.1m (2017: (£0.2m)) to Group results.

On 27 November, Bodycote sold 51% of its shareholding in Techmeta Engineering for consideration of £0.8m. During the year, the Techmeta facility contributed £4.1m (2017: £4.9m) to Group revenue and contributed headline operating profit of £0.2m (2017: £0.4m) to Group results. The remaining 49% shareholding held by Bodycote is disclosed under investment in associate in the consolidated balance sheet.

### Investment in associate

	<b>2018</b>	2017
	<b>£m</b>	£m
Investment in associate	<b>1.4</b>	-
Loan receivable from associate	<b>2.7</b>	-
	<b>4.1</b>	-

Prior to disposal the Group provided an interest bearing credit facility of £3.6m to Techmeta Engineering repayable over 10 years. At the balance sheet date £2.7m remained outstanding.

## 25 Notes to the cash flow statement

	2018 £m	2017 £m
Profit for the year	103.6	97.3
Adjustments for:		
Investment revenue	(0.2)	(0.1)
Finance costs	2.1	2.5
Taxation	28.6	19.7
Depreciation of property, plant and equipment	60.1	58.1
Amortisation of intangible assets	5.6	6.2
Profit on disposal of property, plant and equipment	(1.7)	(0.7)
Share-based payments	3.8	7.8
Impairment of fixed assets	1.8	0.4
Loss on disposal of businesses	0.6	–
EBITDA (See note 1 on page 98)	204.3	191.2
(Increase)/decrease in inventories	(3.9)	0.5
Increase in receivables	(4.0)	(17.0)
Increase in payables	5.1	10.2
Decrease in provisions	(3.7)	(2.1)
Cash generated by operations	197.8	182.8
Income taxes paid	(24.5)	(22.9)
Net cash from operating activities	173.3	159.9
	2018 £m	2017 £m
Cash and cash equivalents comprise:		
Cash and bank balances	38.5	41.0
Bank overdrafts (included in borrowings)	(2.3)	(1.4)
	36.2	39.6

## 26 Operating lease arrangements – the Group as lessee

	2018 £m	2017 £m
Minimum lease payments under operating leases recognised as an expense in cost of sales and overheads	20.2	18.4
At the balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:		
	2018 £m	2017 £m
Within one year	17.1	13.7
In the second to fifth years inclusive	43.9	29.0
After five years	23.1	18.9
	84.1	61.6

Operating lease payments represent rentals payable by the Group for certain of its land and buildings, fixtures and fittings and motor vehicles.

IFRS 16 - Leases, will be effective for accounting periods beginning on or after 1 January 2019. Refer to the Group accounting policies for more information on transition to this standard.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 27 Share-based payments

#### Bodycote Incentive Plan (BIP)

The Company operates the BIP under which executive directors and senior executives receive a conditional award of Bodycote shares up to a maximum of 175% of base salary. Vestings of awards are based upon two performance measures, over a three-year period.

Fifty per cent of the award is subject to a return on capital employed (ROCE) performance condition and 50% of the award is subject to an earnings per share (EPS) performance condition.

In the event that threshold performance for both EPS and ROCE is not achieved, none of the conditional awards will vest.

The number of outstanding share awards is as follows:

	<b>BIP 2018</b>	BIP 2017
At 1 January	<b>2,206,287</b>	2,060,570
Granted during the year	<b>1,043,457</b>	759,058
Exercised during the year	<b>(491,116)</b>	(90,533)
Expired during the year	<b>(246,127)</b>	(522,808)
At 31 December	<b>2,512,501</b>	2,206,287
Average fair value of share awards granted during the year at date of grant (pence)	<b>848.5</b>	757.6
Fair value of awards granted during the year (£)	<b>8,853,733</b>	5,750,623

Exercise Price = £nil.

The inputs to the Black-Scholes simulation model, used to determine the charge to the income statement for BIP, are as follows:

		<b>2018</b>	2017
Weighted average share price	pence	<b>848.5</b>	757.6
Weighted average exercise price	pence	<b>nil</b>	nil
Expected life	years	<b>3.0</b>	3.0
Expected dividend yields	%	<b>3.8</b>	1.9

The Group recognised a total charge to the income statement of £3.8m (2017: £7.8m) related to equity-settled share-based payment transactions.

The Group operated a Co-investment plan (CIP), for which the last award was granted in 2015. The plan is now closed and no shares are outstanding.

### 28 Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

The remuneration of the Board of Directors, who are considered key management personnel of the Group, was as follows:

	<b>2018</b>	2017
	<b>£m</b>	£m
Short-term employee benefits	<b>2.8</b>	3.2
Share-based payments	<b>1.2</b>	0.6
	<b>4.0</b>	3.8

Further information about the remuneration of the individual directors is provided in the Board Report on Remuneration on pages 56 to 77.

## 29 Retirement benefit schemes

### Defined contribution schemes

The Group operates defined contribution retirement benefit schemes for employees in the United Kingdom, France, Belgium, Canada and the United States of America. The assets of the schemes are held separately from those of the Group in funds under the control of trustees. Where there are employees who leave the schemes prior to vesting fully in the contributions, the contributions payable by the Group are reduced by the amount of forfeited contributions.

The Group's employees in Denmark, Finland, Sweden, Italy and the Netherlands are members of state-managed retirement benefit schemes operated by the governments of each country. The relevant subsidiaries are required to contribute a specified percentage of payroll costs to the retirement benefit schemes to fund the benefits. The only obligation of the Group with respect to these retirement benefit schemes is to make the specified contributions.

The total cost charged to income of £7.0m (2017: £6.7m) represents contributions payable to these schemes by the Group at rates specified in the rules of the plans. As at 31 December 2018 contributions of £0.2m (2017: £0.2m) due in respect of the current reporting period had not been paid over to the schemes.

### Defined benefit schemes

The Group operated a number of pension schemes and provided leaving service benefits to certain employees during the year. The defined benefit obligation less fair value of assets at the end of the year and total expense recognised in the income statement are summarised below as follows:

	<b>2018</b>	2017
	<b>£m</b>	£m
UK Scheme	–	(2.4)
Non-UK Schemes	<b>16.8</b>	17.6
	<b>16.8</b>	15.2

### Total expense recognised in income statement

	<b>2018</b>	2017
	<b>£m</b>	£m
UK Scheme	<b>1.6</b>	1.1
Non-UK Schemes	<b>0.4</b>	0.4
	<b>2.0</b>	1.5

### UK Scheme

The Group sponsors the Bodycote UK Pension Scheme ("the Scheme") which is a funded defined benefit arrangement for certain UK employees, and pays out pensions at retirement based on service, final pensionable pay and price inflation. The Scheme is funded by the Group and current employee members. The Scheme exposes the Company to actuarial risks such as longevity risk, interest rate risk and market (investment) risk.

The Scheme operates under UK trust law and the trust is a separate legal entity from the Group. The Scheme is governed by a board of trustees, composed of two member representatives, two employer representatives and one independent trustee. The trustees are required by law to act in the best interests of scheme members and are responsible for setting certain policies (e.g. investment, funding) together with the Group.

Funding of the Scheme is based on a separate actuarial valuation for funding purposes for which the assumptions may differ from the assumptions above. Funding requirements are formally set out in the Statement of Funding Principles, Schedule of Contributions and Recovery Plan agreed between the Trustees and the Group. The actuarial valuation of the Scheme as at 6 April 2018 was completed by a qualified independent actuary and the results of this have been updated on an approximate basis to 31 December 2018.

The contributions made by the employer over the financial year have been £0.7m, comprising £0.3m in respect of benefit accrual and £0.4m in respect of ongoing expenses.

It is the policy of the Group to recognise all actuarial gains and losses in the year in which they occur outside of the profit and loss account and in Other Comprehensive Income.

As the Group does not have an unconditional right to a return of any surplus in the Scheme under the wording of the Scheme Rules, the additional reporting requirements of IFRIC 14 apply. As the Scheme is in surplus as at 31 December 2018 a restriction must be applied to the balance sheet. The surplus recognised on the balance sheet has been restricted to £nil. No further liabilities need to be recognised at 31 December 2018 as the Group is not committed to paying any further deficit reduction contributions under the current Schedule of Contributions.

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 29 Retirement benefit schemes continued

### Reconciliation of opening and closing balances of the present value of the defined benefit obligation

	2018	2017
	£m	£m
Defined benefit obligation at start of year	109.9	126.6
Current service cost	0.6	0.6
Interest expense	2.4	2.9
Contributions by plan participants	0.1	0.1
Actuarial gains arising from changes in demographic assumptions	(0.7)	(2.4)
Actuarial (gains)/losses arising from changes in financial assumptions	(7.1)	0.6
Experience gains on liabilities	–	(5.4)
Benefits paid, death in service insurance premiums and expenses	(5.7)	(13.1)
Past service cost	0.7	–
Defined benefit obligation at end of year	<b>100.2</b>	109.9

### Reconciliation of opening and closing balances of the fair value of the assets

	2018	2017
	£m	£m
Fair value of assets at start of year	117.5	123.0
Interest income	2.6	2.8
Return on scheme assets excluding interest income	(3.8)	4.4
Scheme administration expenses	(0.4)	(0.4)
Contributions by employer	0.7	0.7
Contributions by plan participants	0.1	0.1
Benefits paid, death in service insurance premiums and expenses	(5.7)	(13.1)
Fair value of assets at end of year	<b>111.0</b>	117.5

### Total expense recognised in the income statement

	2018	2017
	£m	£m
Current service cost	0.6	0.6
Past service cost	0.7	–
Net interest on the defined benefit (asset)/liability	(0.1)	0.1
Scheme administration expenses	0.4	0.4
Total expenses	<b>1.6</b>	1.1

### Assets

	2018	2018	2017	2017
	Quoted	Unquoted	Quoted	Unquoted
	£m	£m	£m	£m
Equities	–	–	14.4	–
Bonds	78.9	9.8	60.9	15.4
Cash	9.1	–	5.1	–
Diversified growth funds	–	–	7.9	–
Diversified credit funds	–	13.2	13.8	–
	<b>88.0</b>	<b>23.0</b>	102.1	15.4

None of the fair value of the assets shown above include any of the Group's own financial instruments or any property occupied by, or other assets used by the Group.

The Scheme's present strategic target is to allocate 72.5% of the investment portfolio to 'non-LDI' asset classes which includes credit-based investments, such as semi-liquid credit, corporate bonds and absolute return bonds and 27.5% to 'liability-matching' asset classes, namely Liability Driven Investment ('LDI'). The LDI portion of assets has been put in place to reduce interest rate and inflation risk.

## 29 Retirement benefit schemes continued

### Assumptions

	2018 % per annum	2017 % per annum
RPI inflation	3.25	3.25
CPI inflation	2.45	2.45
Salary increases	3.00	3.00
Rate of discount	2.65	2.25
Allowance for pension in payment increases of RPI or 3% p.a. if less	2.41	2.41
Allowance for revaluation of deferred pensions	2.45	2.45

Mortality – current pensioners:

	2018 S2PxA YoB CMI 2017 1.5% long term trend	2017 S2PxA YoB CMI 2016 1.5% long-term trend
Actuarial tables used		
Life expectancy for members currently aged 65	22.4	22.6

Mortality – future pensioners:

	2018 S2PxA YoB CMI 2017 1.5% long term trend	2017 S2PxA YoB CMI 2016 1.5% long-term trend
Actuarial tables used		
Life expectancy at age 65 for members currently aged 40	24.2	24.3

	2018 All members commute 75% of maximum permitted	2017 All members commute 75% of maximum permitted
Cash commutation		

The weighted average duration of the defined benefit obligation as at 31 December 2018 is approximately 18 years (31 December 2017: 19 years).

### Present value of defined benefit obligations, fair value of (assets) and deficit

	2018 £m	2017 £m
Present value of defined benefit obligation	100.2	109.9
Fair value of plan assets	(111.0)	(117.5)
Surplus in the Scheme	(10.8)	(7.6)
Adjustment relating to asset ceilings and minimum funding requirements	10.8	5.2
Net defined benefit asset before deferred tax	–	(2.4)

### Reconciliation of asset ceiling

	2018 £m	2017 £m
Restriction due to asset ceiling at beginning of period	5.2	–
Interest on asset restriction	0.1	–
Other changes in asset restriction	5.5	5.2
Restriction due to asset ceiling at end of period	10.8	5.2

The best estimate of contributions to be paid into the plan for the year ending 31 December 2018 is £0.8m.

# Notes to the consolidated financial statements continued

Year ended 31 December 2018

## 29 Retirement benefit schemes continued

### Amounts recognised in Other Comprehensive Income

	2018 £m	2017 £m
Gain on experience on plan liabilities	–	5.4
Return on scheme assets excluding interest income	(3.8)	4.4
Effects of changes in financial assumptions underlying the present value of the liabilities	7.1	(0.6)
Effects of changes in demographic assumptions underlying the present value of the liabilities	0.7	2.4
Loss due to change in asset restriction	(5.5)	(5.2)
<b>Total (loss)/gain recognised in Other Comprehensive Income</b>	<b>(1.5)</b>	<b>6.4</b>

### Impact of changes to assumptions

	2018		2017	
	Increase £m	Decrease £m	Increase £m	Decrease £m
0.25% change in discount rate	(4.3)	4.3	(4.9)	4.9
0.25% change in price inflation (and associated assumptions)	1.7	(1.7)	1.8	(1.8)
1 year change in life expectancy at age 65	3.2	(3.2)	4.4	(4.4)

### Combined non-UK disclosures

The Group operates schemes in the USA and continental Europe.

In Europe the Group operates defined benefit pension, post retirement and long-service arrangements for certain employees in France, Germany, Italy, Turkey, Switzerland and Liechtenstein.

### Reconciliation of opening and closing balances of the present value of the defined benefit obligation

	2018 £m	2017 £m
Defined benefit obligation at start of year	27.3	29.0
Current service cost	0.7	0.7
Interest expense	0.4	0.5
Actuarial (gains)/losses arising from changes in financial assumptions	(1.1)	0.2
Experience gains on liabilities	(0.3)	(0.3)
Benefits paid, death in service insurance premiums and expenses	(1.0)	(2.1)
Employee contributions	0.1	0.1
Settlements	(0.6)	(2.7)
Past service cost	–	2.1
Exchange rate loss/(gain)	0.8	(0.2)
<b>Defined benefit obligation at end of year</b>	<b>26.3</b>	<b>27.3</b>



## 29 Retirement benefit schemes continued

### Reconciliation of opening and closing balances of the fair value of plan assets

	2018 £m	2017 £m
Fair value of assets at start of year	9.7	11.1
Interest income	0.1	0.2
Return on scheme assets excluding interest income	(0.7)	0.2
Contributions by employer	0.2	0.2
Contributions by employees	0.1	0.1
Benefits paid, death in service insurance premiums and expenses	(0.4)	(1.4)
Settlements	–	(1.9)
Past service credit	–	1.9
Exchange rate gain/(loss)	0.5	(0.7)
Fair value of assets at end of year	<b>9.5</b>	9.7

### Total expense recognised in the income statement

	2018 £m	2017 £m
Current service cost	0.7	0.7
Net interest on the defined benefit liability	0.3	0.3
Settlements	(0.6)	(0.8)
Past service cost	–	0.2
Total expense	<b>0.4</b>	0.4

### Assets

	2018		2017	
	Quoted £m	Unquoted £m	Quoted £m	Unquoted £m
Equities	3.7	–	3.8	–
Cash and cash equivalents	–	–	–	0.2
Insurance contracts	–	5.8	–	5.7
Total	<b>3.7</b>	<b>5.8</b>	3.8	5.9

None of the fair values of the assets shown above include any of the Group's own financial instruments or any property occupied by, or other assets used by, the Group.

# Notes to the consolidated financial statements continued

## Year ended 31 December 2018

### 29 Retirement benefit schemes continued

#### Assumptions for 2018

	Salary increases % per annum	Rate of discount % per annum	Inflation % per annum	Pension increases % per annum
USA – non-metallurgical	n/a	4.3	n/a	n/a
France	2.5	1.6	1.5	1.0
Germany	2.5	2.0	n/a	1.8
Italy	2.5	1.5	1.5	n/a
Turkey	8.0	13.5	8.0	n/a
Liechtenstein	2.5	1.0	n/a	n/a
Switzerland	n/a	1.0	n/a	n/a

#### Duration

The weighted average durations of the defined benefit obligations of the overseas schemes at 31 December 2018 range from 11 years to 19 years. The durations ranged from 13 years to 19 years as at 31 December 2017.

#### Present value of defined benefit obligations, fair value of assets and deficit

	2018 £m	2017 £m
Present value of defined benefit obligation	26.3	27.3
Fair value of plan assets	(9.5)	(9.7)
Deficit in the schemes	16.8	17.6

As all actuarial gains and losses are recognised, the deficit shown above at 31 December 2018 is that recognised in the balance sheet.

#### Amounts recognised in Other Comprehensive Income

	2018 £m	2017 £m
Gain from experience on plan liabilities	0.3	0.3
Return on scheme assets excluding interest income	(0.7)	0.2
Effects of changes in financial assumptions underlying the present value of the liabilities	1.1	(0.2)
Total gain recognised in Other Comprehensive Income	0.7	0.3

The only funded plans are those operated in the USA, France, Switzerland and Liechtenstein. The best estimate of contributions to be paid into the plans for the year ending 31 December 2018 is £0.2m.

#### Sensitivities (changes to total defined benefit obligations)

	2018		2017	
	Increase £m	Decrease £m	Increase £m	Decrease £m
0.25% change in discount rate	(0.9)	0.9	(1.0)	1.0
0.25% change in price inflation (and associated assumptions)	0.5	(0.5)	0.5	(0.5)

### 30 Contingent liabilities

The international tax environment has received increased attention and seen rapid change over recent years, both at a US and European level, and by international bodies such as the Organisation for Economic Cooperation and Development (OECD). Against this backdrop, Bodycote has been monitoring developments and continues to engage transparently with the tax authorities in the countries where we operate. In October 2017, the European Commission opened a state aid investigation into the Group Financing Exemption in the UK-controlled foreign company rules. The Group Financing Exemption was introduced in legislation by the British Government in 2013. In common with other UK-based international companies whose arrangements are in line with current UK CFC legislation, Bodycote may be affected by the outcome of this investigation. If the preliminary findings of the European Commission's investigation into the UK legislation are upheld, we calculate the maximum potential liability to be approximately £20.0m (2017: £15.0m). Based on a current assessment, Bodycote believes that no provision is required in respect of this matter.

# Five year summary

	2018 £m	2017 £m	2016 £m	2015 £m	2014 £m
<b>Revenue</b>	<b>728.6</b>	690.2	600.6	567.2	609.1
<b>Profit:</b>					
<b>Headline operating profit</b>	<b>138.3</b>	123.9	99.6	102.1	111.1
Amortisation of acquired intangible fixed assets	<b>(3.7)</b>	(4.5)	(4.5)	(4.2)	(3.9)
Acquisition costs	<b>(0.5)</b>	–	(0.6)	–	(0.2)
<b>Operating profit prior to exceptional items</b>	<b>134.1</b>	119.4	94.5	97.9	107.0
Reorganisation costs	–	–	–	(20.0)	–
<b>Operating profit</b>	<b>134.1</b>	119.4	94.5	77.9	107.0
Net finance costs	<b>(1.9)</b>	(2.4)	(2.6)	(2.9)	(3.3)
<b>Profit before taxation</b>	<b>132.2</b>	117.0	91.9	75.0	103.7
Taxation	<b>(28.6)</b>	(19.7)	(24.9)	(18.8)	(24.4)
<b>Profit after taxation</b>	<b>103.6</b>	97.3	67.0	56.2	79.3
Non-controlling interests	<b>(0.4)</b>	(0.2)	–	–	0.1
<b>Profit attributable to the equity holders of the parent</b>	<b>103.2</b>	97.1	67.0	56.2	79.4
Headline earnings per share (pence)	<b>55.9</b>	49.2	37.0	39.5	43.8
Dividend per share (pence)	<b>19.0</b>	17.4	15.8	15.1	14.4
Special dividend per share (pence)	<b>20.0</b>	25.0	–	10.0	20.0
<b>Assets employed</b>					
Intangible fixed assets	<b>206.9</b>	201.0	206.7	175.2	172.1
Tangible fixed assets	<b>546.6</b>	520.5	509.0	429.6	434.6
Other assets and liabilities	<b>(63.1)</b>	(63.6)	(88.5)	(67.5)	(71.5)
	<b>690.4</b>	657.9	627.2	537.3	535.2
<b>Financed by</b>					
Share capital	<b>33.1</b>	33.1	33.1	33.1	33.1
Reserves	<b>692.8</b>	663.9	594.8	516.1	537.3
<b>Shareholders' funds</b>	<b>725.9</b>	697.0	627.9	549.2	570.4
Non-controlling interests	<b>0.7</b>	0.5	0.4	0.4	0.5
Net cash	<b>(36.2)</b>	(39.6)	(1.1)	(12.3)	(35.7)
<b>Capital employed</b>	<b>690.4</b>	657.9	627.2	537.3	535.2
<b>Net assets per share (pence)</b>	<b>379.1</b>	364.1	328.0	286.9	297.9
<b>Return on capital employed (%):</b>					
Headline operating profit divided by the average of opening and closing capital employed as adjusted for certain items of goodwill written off	<b>20.5</b>	19.3	17.1	19.0	20.7

# Company statement of financial position

At 31 December 2018

	Note	2018 £m	2017 £m
<b>Fixed assets</b>			
Intangible fixed assets	2	22.3	22.2
Tangible fixed assets	3	0.1	0.2
Investments	4	391.0	390.9
Receivables	5	2.9	16.3
Retirement benefit assets	11	–	2.4
		<b>416.3</b>	432.0
<b>Current assets</b>			
Receivables	5	7.8	1.5
<b>Current liabilities</b>			
Payables	6	(14.3)	(13.0)
<b>Net current liabilities</b>		<b>(6.5)</b>	(11.5)
<b>Total assets less current liabilities</b>		<b>409.8</b>	420.5
Payables: Amounts falling due after more than one year	6	(11.5)	–
<b>Net assets</b>		<b>398.3</b>	420.5
<b>Capital and reserves</b>			
Called-up share capital	8	33.1	33.1
Share premium account		177.1	177.1
Other reserves		126.3	133.6
Profit for the year		67.7	28.7
Retained earnings		(5.9)	48.0
<b>Shareholders' funds</b>		<b>398.3</b>	420.5

The financial statements of Bodycote plc, registered number 519057, were approved by the Board of Directors and authorised for issue on 8 March 2019.

They were signed on its behalf by:

**S.C. Harris**  
Director

**D. Yates**  
Director

# Company statement of changes in equity

For the year ended 31 December 2018

	Called-up share capital £m	Share premium account £m	Other reserves £m	Profit and loss account £m	Total £m
1 January 2017	33.1	177.1	125.0	74.1	409.3
Profit for the year	–	–	–	28.7	28.7
Actuarial loss on defined benefit pension schemes net of deferred tax	–	–	–	5.4	5.4
Other comprehensive income	–	–	–	–	–
<b>Total comprehensive income for the year</b>	–	–	–	34.1	34.1
Dividends paid	–	–	–	(30.6)	(30.6)
Share-based payments	–	–	7.8	–	7.8
Acquisition of own shares	–	–	–	–	–
Settlement of share options	–	–	0.8	(0.9)	(0.1)
<b>31 December 2017</b>	<b>33.1</b>	<b>177.1</b>	<b>133.6</b>	<b>76.7</b>	<b>420.5</b>
Profit for the year	–	–	–	67.7	67.7
Actuarial loss on defined benefit pension schemes net of deferred tax	–	–	–	(1.3)	(1.3)
<b>Total comprehensive income for the year</b>	–	–	–	66.4	66.4
Dividends paid	–	–	–	(81.8)	(81.8)
Shares acquired	–	–	(10.6)	–	(10.6)
Share-based payments	–	–	3.8	–	3.8
Settlement of share options	–	–	(0.5)	0.5	–
<b>31 December 2018</b>	<b>33.1</b>	<b>177.1</b>	<b>126.3</b>	<b>61.8</b>	<b>398.3</b>

Details of dividends paid are set out in note 7 to the consolidated financial statements.

Details of share-based payment transactions are set out in note 27 of the consolidated financial statements.

The other reserves are stated after deducting £7.2m (2017: £8.0m) relating to shares held in the Bodycote International Employee Benefit Trust. The Bodycote International Employee Benefit Trust holds Bodycote plc shares and satisfies awards made under various employee incentive schemes when issuance of new shares is not appropriate.

At 31 December 2018 1,839,860 (2017: 1,171,190) ordinary shares of 17 3/11p each were held by the Bodycote International Employee Benefit Trust and, following recommendations by the employer, are provisionally allocated to satisfy awards under employee incentive schemes. The trust waives payment of dividend. The market value of these shares was £13.4m (2017: £10.7m).

Included in other reserves £10.8m (2017: £10.4m) relating to the share option reserve and the capital redemption reserve of £129.8m (2017: £129.8m).

# Company accounting policies

## Accounting convention

The financial statements have been prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101) and in accordance with applicable accounting standards. The financial statements have been prepared under the historical cost convention and in accordance with applicable law. The principal accounting policies are summarised below. They have all been applied consistently throughout the year and the preceding year in dealing with items that are considered material in relation to the Company's financial statements. In accordance with Section 408 of the Companies Act 2006, a separate profit and loss account dealing with the results of the Company has not been presented.

As permitted by FRS 101, the Company has taken advantage of the disclosure exemptions available under that standard in relation to share-based payments, financial instruments, capital management, presentation of a cash flow statement, presentation of comparative information in respect of certain assets, standards not yet effective, impairment of assets, business combinations, discontinued operations and related party transactions.

Where required, equivalent disclosures are given in the consolidated financial statements.

## Going concern

The directors have at the time of approving the financial statements a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Thus, they continue to adopt the going concern basis of accounting in preparing the financial statements. Further detail is contained in the Chief Financial Officer's report on page 26.

## Investments

Investments are held at cost less provision for impairment, if any.

## Foreign currencies

Transactions in currencies other than pounds sterling are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated. Gains and losses arising on retranslation are included in net profit or loss for the period.

## Pension costs

The Company participates in a final salary defined benefit pension scheme in the United Kingdom which is funded by the payment of contributions to a separately administered trust fund. This is a defined benefit plan which shares the risks between entities under common control. For further details, see note 11.

There is no contractual arrangement or policy for charging the net benefit cost between the entities who participate in this scheme. The Company is considered to be the entity that is legally the sponsoring employer of this scheme. As such, the Company recognises the net defined benefit cost and the retirement benefit obligation as per the requirements of IAS 19 Employee Benefits, as described in further detail in the accounting policies of the consolidated financial statements on page 93.

For defined contribution schemes, the amount charged to the profit and loss account in respect of pension costs is the contributions payable in the year.

## Leases

Rental costs under operating leases are charged to the profit and loss account on a straight-line basis over the period of the lease.

### Tangible fixed assets

Tangible fixed assets are stated at cost net of depreciation and any provision for impairment. Depreciation is provided on a straight-line basis, to reduce the carrying value to the estimated residual value at the point of sale, at the following annual rates:

Fixtures and fittings            10% to 20%

### Intangible fixed assets

Intangible fixed assets are stated at cost net of amortisation and any provision for impairment. Amortisation is provided on a straight-line basis over their estimated useful lives, at the following annual rates:

Software                            10% to 33%

### Taxation

Current UK corporation tax and foreign tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is recognised in respect of all temporary differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date. Temporary differences are differences between the Company's taxable profits and its results as stated in the financial statements that arise from the inclusion of gains and losses in tax assessments in periods different from those in which they are recognised in the financial statements.

A net deferred tax asset is regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits from which the future reversal of the underlying temporary differences can be deducted.

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the temporary differences are expected to reverse based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date.

### Related party transactions

The Company has taken advantage of the exemption contained in FRS 8 Related Party Transactions not to disclose transactions or balances with wholly-owned entities of the Group.

### Share-based payments

The Company has applied the requirements of IFRS 2 Share-based Payment.

The Company issues equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period. At each balance sheet date, the Company revises its estimate of the number of equity instruments expected to vest as a result of the effect of non-market based vesting conditions. The impact of the revision of the original estimates, if any, is recognised in profit or loss such that the cumulative expense reflects the revised estimates with a corresponding adjustment to the equity-settled employee benefits reserve.

### Critical judgements in applying the Company's accounting policies and key sources of estimation uncertainty

In the course of preparing the Company's financial statements, no judgement or key source of estimation uncertainty has been identified.

# Notes to the company financial statements

Year ended 31 December 2018

## 1 Profit for the year

Bodycote plc reported a profit for the financial year ended 31 December 2018 of £67.7m (2017: £28.7m).

The auditor's remuneration for audit and other services is disclosed in note 3 to the consolidated financial statements.

Disclosure of individual directors' remuneration, share interests, share options, long-term incentive schemes, pension contributions and pension entitlements required by the Companies Act 2006 and those specified for audit by the Listing Rules of the Financial Conduct Authority are shown in the tables in the Board report on remuneration on pages 56 to 77 and form part of these financial statements.

## 2 Intangible fixed assets

	Software £m
<b>Cost</b>	
At 1 January 2018	29.8
Additions	1.7
<b>At 31 December 2018</b>	<b>31.5</b>
<b>Amortisation</b>	
At 1 January 2018	7.6
Charge for the year	1.6
<b>At 31 December 2018</b>	<b>9.2</b>
<b>Net book value</b>	
<b>At 31 December 2018</b>	<b>22.3</b>
At 31 December 2017	22.2

Refer to note 10 to the consolidated financial statements for more information.

## 3 Tangible fixed assets

	Fixtures and fittings £m
<b>Cost</b>	
<b>At 1 January 2018 and 31 December 2018</b>	<b>0.9</b>
<b>Depreciation</b>	
At 1 January 2018	0.7
Charge for the year	0.1
<b>At 31 December 2018</b>	<b>0.8</b>
<b>Net book value</b>	
<b>At 31 December 2018</b>	<b>0.1</b>
At 31 December 2017	0.2



## 4 Investments

	Shares £m
<b>Cost</b>	
At 1 January 2018	397.5
Acquisitions	0.1
<b>At 31 December 2018</b>	<b>397.6</b>
<b>Provision for impairment</b>	
At 1 January 2018	6.6
<b>At 31 December 2018</b>	<b>6.6</b>
<b>Net book value</b>	
<b>At 31 December 2018</b>	<b>391.0</b>
At 31 December 2017	390.9

During 2018 the Company subscribed CHF 100,000 (£76,000) in Bodycote (Suisse) SA.

The following subsidiaries have taken advantage of an exemption from audit under section 479A of the Companies Act 2006. As the ultimate parent, Bodycote plc has provided a statutory guarantee for any outstanding liabilities of this business. All subsidiaries undertakings have been included in the consolidation.

Bodycote Heat Treatments Limited  
 Bodycote Surface Technology Limited  
 Bodycote H.I.P. Limited  
 Bodycote America Finance Limited  
 Bodycote America Treasury Limited  
 Bodycote Finance Limited  
 Bodycote Finance UK Limited  
 Bodycote International Limited  
 Bodycote Investments  
 Bodycote Nominees No. 1 Limited  
 Bodycote Pension Trustees Limited  
 Bodycote HIP Germany Limited  
 Bodycote Treasury Services Limited  
 Bodycote Thermal Processing Mexico Limited

## 5 Receivables

	2018 £m	2017 £m
<b>Amounts falling due within one year:</b>		
Amounts owed by subsidiary undertakings	6.5	0.7
Corporation tax recoverable	1.0	–
Other receivables and prepayments	0.3	0.8
	<b>7.8</b>	1.5
<b>Amounts falling due after more than one year:</b>		
Amounts owed by subsidiary undertakings	2.6	15.8
Deferred taxation (note 7)	0.3	0.5
	<b>2.9</b>	16.3
	<b>10.7</b>	17.8

# Notes to the company financial statements continued

Year ended 31 December 2018

## 6 Payables

	2018 £m	2017 £m
<b>Amounts falling due within one year:</b>		
Trade payables	0.6	0.8
Amounts owed to subsidiary undertakings	0.8	0.5
Other taxes and social security	3.4	1.8
Other payables	4.3	4.8
Accruals and deferred income	5.2	5.1
	<b>14.3</b>	13.0
<b>Amounts falling due after more than one year:</b>		
Amounts owed to subsidiary undertakings <sup>1</sup>	11.5	–

1. Intercompany loan to Bodycote Finance Limited.

## 7 Deferred tax assets

The following are the major deferred tax assets recognised by the Company and movements thereon during the current and prior reporting period.

	Retirement benefit obligations £m	Other timing differences £m	Total £m
At 1 January 2017	0.6	0.3	0.9
Credit to profit or loss	0.1	0.1	0.2
Credit to other comprehensive income	(1.1)	–	(1.1)
At 1 January 2018	(0.4)	0.4	–
Credit to other comprehensive income	(0.1)	–	(0.1)
<b>At 31 December 2018</b>	<b>(0.5)</b>	<b>0.4</b>	<b>(0.1)</b>

Deferred tax assets and liabilities are offset where the Company has a legally enforceable right to do so. The following is the analysis of the deferred tax balances (after offset) for financial reporting purposes:

	2018 £m	2017 £m
Deferred tax assets	0.3	0.9

## 8 Called-up share capital

### Share capital:

#### Ordinary shares (allotted, called-up and fully paid)

	Number of shares	£m
At 1 January 2018	191,456,172	33.1
<b>At 31 December 2018</b>	<b>191,456,172</b>	<b>33.1</b>

Details of share options in issue on the Company's share capital and share-based payments are set out in note 27 to the consolidated financial statements.

## 9 Contingent liabilities

The Company has guaranteed bank overdrafts, loans and letters of credit of certain subsidiary undertakings amounting to £9.1m (2017: £8.9m).

## 10 Operating lease arrangements – the Company as lessee

	2018	2017
	£m	£m
Minimum lease payments under operating leases recognised as an expense	<b>0.3</b>	0.3

At the balance sheet date, the Company had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2018	2017
	£m	£m
Within one year	<b>0.2</b>	0.2
In the second to fifth years inclusive	<b>0.7</b>	0.1
	<b>0.9</b>	0.3

Operating lease payments represent rentals payable by the Company for its land and buildings and motor vehicles.

## 11 Pension commitments

The Company participates in a final salary defined benefit scheme, the details of which are disclosed in note 29 to the consolidated financial statements. This is a defined benefit plan which shares the risks between entities under common control. There is no contractual agreement or policy for charging the net benefit cost between entities who participate in this scheme. The Company is considered to be the entity that is legally the sponsoring employer of this scheme. The net defined benefit cost and the retirement benefit obligation are recognised as per the requirements of IAS 19 (revised) Employee Benefits. Full disclosures concerning the scheme as required by IAS 19 (revised) are set out in note 29 to the consolidated financial statements.

The contributions made by the Company over the financial year to the defined contribution scheme amounted to £0.3m (2017: £0.3m). As at 31 December 2018, contributions of £nil (2017: £nil) due in respect of the current reporting period had not been paid over to the scheme.

## 12 Related party transactions

During the current and prior year, the Company has not entered into any transactions with related parties who are not wholly-owned members of the Group.

# Subsidiary undertakings

## Incorporated in the UK

### **Springwood Court, Springwood Close, Tytherington Business Park, Macclesfield SK10 2XF**

Bodycote America Finance Limited<sup>6</sup>  
Bodycote America Treasury Limited<sup>6</sup>  
Bodycote Developments Limited<sup>2, 4</sup>  
Bodycote Finance Limited<sup>6</sup>  
Bodycote Finance UK Limited<sup>6</sup>  
Bodycote Heat Treatments Limited<sup>1</sup>  
Bodycote H.I.P. Limited<sup>1</sup>  
Bodycote HIP Germany Limited<sup>3</sup>  
Bodycote International Limited<sup>3</sup>  
Bodycote Investments<sup>6</sup>  
Bodycote K-Tech Limited<sup>2</sup>  
Bodycote Nominees No. 1 Limited<sup>2</sup>  
Bodycote Nominees No. 2 Limited<sup>2</sup>  
Bodycote Pension Trustees Limited<sup>5</sup>  
Bodycote Processing (Skelmersdale) Limited<sup>2, 4</sup>  
Bodycote Surface Technology Limited<sup>1</sup>  
Bodycote Thermal Processing Limited<sup>2</sup>  
Bodycote Thermal Processing Mexico Limited<sup>1</sup>  
Bodycote Treasury Services Limited<sup>6</sup> – ordinary and preference shares  
Expert Heat Treatments Limited<sup>2, 4</sup>  
Taylor & Hartley Fabrics Limited<sup>2</sup>

## Incorporated in Belgium

### **Font Saint Landry 11, 1120 Brussels, Belgium**

Bodycote Belgium SA<sup>1</sup>

### **Industrie Park Noord 7, 9100 Sint-Niklaas, Belgium**

Bodycote Hot Isostatic Pressing NV<sup>1</sup>

## Incorporated in Canada

### **630 Newpark Boulevard, Newmarket ON L3X 2S2, Canada**

Bodycote Canada Property Inc.<sup>4</sup>  
Bodycote Thermal Processing Canada, Inc.<sup>1</sup>

### **50 Queen Street North, Suite 1020, Kitchener ON N2H 6M2, Canada**

Bodycote Heat Treatment Canada, Inc.<sup>1</sup>

## Incorporated in China

### **No. 68 Ningbo East Road, Taicang Economic Development Area, Taicang City, Jiangsu, China**

Bodycote Heat Treatments Technology (Taicang) Co., Limited<sup>1</sup>

### **2012 Kehang Road, High Tech District, Jinan City, Shandong, China**

Bodycote (Jinan) Heat Treatments Technology Co., Ltd.<sup>1</sup>

### **No.12 Building, No. 78, Gu Cheng Zhong Road, Yu Shan Town, Kunshan City, Jiangsu Province, China**

Bodycote (Kunshan) Heat Treatments Technology Co., Ltd.<sup>1</sup>

### **No.B2-A, Wuxi National Hi-New Tech Industrial Development Z, Wuxi City, Jiangsu Province, 214028, China**

Bodycote Wuxi Technology Co., Ltd.<sup>1</sup>

## Incorporated in Czech Republic

### **Liberec 30, Tanvaldska 345, PSC, 46311, Czech Republic**

Bodycote HT s.r.o<sup>1</sup>

### **Rohanske nabrezi 671/15, Karlín, 186 00, Praha 8, Czech Republic**

Bodycote SSC s.r.o<sup>6</sup>

## Incorporated in France

**Ilena Park – Bât. B2, Parc Technologique de Lyon, 117, allée des Parcs, 69800 Saint Priest, France**

Bodycote Bourgogne SAS<sup>1</sup>  
 Bodycote France Holdings SA<sup>3</sup>  
 Bodycote Haute-Savoie SAS<sup>2</sup>  
 Bodycote Lyon SNC<sup>6</sup>  
 Bodycote Metz-Tessy SAS<sup>1</sup>  
 Bodycote SAS<sup>1</sup>  
 Bodycote Sud-Ouest SAS<sup>1</sup>  
 HITEC SAS<sup>2</sup>  
 Nitruvid SAS<sup>1</sup>

## Incorporated in Germany

**Schiessstrasse 68, 40549 Düsseldorf, Germany**

Bodycote Deutschland GmbH<sup>6</sup>  
 Bodycote European Holdings GmbH<sup>3</sup>  
 Bodycote Germany – East GmbH<sup>6</sup>  
 Bodycote Hirzenhain GmbH<sup>1</sup>  
 Bodycote Specialist Technologies GmbH<sup>1</sup>  
 Bodycote Specialist Technologies Deutschland GmbH<sup>1</sup>  
 Bodycote VHK Vakuum-Härtereie Köllner GmbH<sup>1</sup>  
 Bodycote Wärmebehandlung GmbH<sup>1</sup>

## Incorporated in Ireland

**12 Merrion Square North, Dublin 2, Ireland**

Bodycote Ireland Finance DAC<sup>6</sup>  
 Bodycote Ireland Treasury Limited<sup>6</sup>

## Incorporated in Mexico

**Oficinas en el Parque Torre Baker & McKenzie, Piso 10, Blvd. Antonio L. Rodríguez 1884 Pte, Monterrey, NL, 64650, Mexico**

Bodycote de Mexico, S. de R.L. de C.V.<sup>1</sup>  
 Bodycote de SLP, S. de R.L. de C.V.<sup>1</sup>  
 Bodycote Testing de Mexico, S. de R.L. de C.V.<sup>2</sup>  
 Bodycote Thermal Processing de Mexico, S. de R.L. de C.V.<sup>1</sup>  
 Bodycote Thermal Processing de Mexico Servicios, S. de R.L. de C.V.<sup>6</sup>

## Incorporated in Sweden

**Box 209, 735 23 Surahammar, Sweden**

Bodycote Hot Isostatic Pressing AB<sup>1</sup>  
 Box 124, 424 23, Angered, Sweden  
 Bodycote Sweden AB<sup>3</sup>  
 Bodycote Thermotreat AB<sup>2</sup>  
 Bodycote Värmebehandling AB<sup>1</sup>  
 Bodycote Ytbehandling AB<sup>1</sup>

## Incorporated in USA

**12700 Park Central Drive, Suite 700, Dallas TX 75251-1518, USA**

Bodycote Americas, Inc.<sup>3</sup>  
 Bodycote IMT, Inc.<sup>1</sup>  
 Bodycote K-Tech, Inc.<sup>1</sup>  
 Bodycote Syracuse Heat Treating Corporation<sup>1</sup>  
 Bodycote Thermal Processing, Inc.<sup>1</sup>  
 Bodycote USA, Inc.<sup>3</sup>

**1180 Enterprise Dr, Winchester, KY 40391, USA**

Bodycote Winchester, Inc.<sup>1</sup>

# Subsidiary undertakings continued

## Incorporated in other overseas countries

### **Boehlerdurplatz 1, 8605 Kapfenberg, Austria**

Bodycote Austria GmbH<sup>1</sup>

### **Groethofstraat 27, 5916PA Venlo, Netherlands**

Bodycote Hardingscentrum BV<sup>1</sup>

### **Orczy ut 46, Budapest, H-1089, Hungary**

Bodycote Hungary Hökezelő KFT<sup>1</sup>

### **Kemalpasa OSB, Izmir Kemalpasa Asfalti No:17/1, 35730 Kemalpasa-IZMIR, Turkey**

Bodycote Istas Isil Islem Sanayi ve Ticaret AS (79.3% owned)<sup>1</sup>

### **50 La Colomberie, St Helier, JE2 4QB, Jersey**

Bodycote Jersey Holdings Limited<sup>3</sup>

### **Gesällvägen 7, 01730 Vantaa, Finland**

Bodycote Lämpökäsittely Oy<sup>1</sup>

### **7, Rue Robert Stumper, L-2557 Luxembourg**

Bodycote Luxembourg Finance SARL<sup>6</sup>

### **Wilgowa 65D, Czystochowa, 42-271, Poland**

Bodycote Polska sp z.o.o.<sup>1</sup>

### **Im alten Riet 123, 9494 Schaan, Liechtenstein**

Bodycote Rheintal Wärmebehandlung AG<sup>1</sup>

### **Avenue Perdtemps 23, 1260 Nyon, Switzerland**

Bodycote (Suisse) SA<sup>6</sup>

### **Via Moie 28, 25050, Rodengo Saiano, Italy**

Bodycote Trattamenti Termici SpA<sup>1</sup>

### **Brasov, str. Zizinului nr. 119, cod 500407, Romania**

Bodycote Tratamente Termice SRL<sup>1</sup>

### **Industribuen 16-18, 5592, Ejby, Denmark**

Bodycote Varmebehandling A/S<sup>1</sup>

## Other:

### Incorporated in France

#### **Lieu-dit Champ Corbert, 74370, Metz Tassy, France**

Techmeta Engineering SAS (49% Investment)

### Incorporated in USA

#### **13753 Otterson Court, Livonia, MI 48150, USA**

Thixomat Technologies, LLC (13.9% Investment)

## Classifications Key

1. Thermal processing company
2. Dormant
3. Holding company
4. Property holding company
5. Trustee
6. Provision of services to Group companies

Except where stated, these companies are wholly-owned subsidiaries and have only one class of issued shares.

It is agreed that the six German subsidiaries Bodycote European Holdings GmbH, Bodycote Hirzenhain GmbH, Bodycote Specialist Technologies Deutschland GmbH, Bodycote Specialist Technologies GmbH, Bodycote VHK Vakuum-Härtereie Köllner GmbH and Bodycote Wärmebehandlung GmbH make use of the exemption option under Sec. 264 para. 3 German Commercial Code for the fiscal year 2018, and will not publish their annual financial statements according to Sec. 325 et seq. German Commercial Code.

It is also agreed that the Dutch subsidiary Bodycote Hardingscentrum BV makes use of the exemption under Article 403, paragraph 1 of Book 2 Dutch Civil Code and will not publish its annual financial statements.

The financial data of the above German and Dutch companies for 2018 are included in the consolidated annual accounts of Bodycote plc.

# Shareholder enquiries

Enquiries on the following administrative matters can be addressed to the Company's registrars at Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex BN99 6DA. Telephone 0333 207 5951 (+44 121 415 0804 if calling from outside the UK). Lines open 8.30am to 5.30pm (UK time), Monday to Friday excluding public holidays in England and Wales. Email: Log on to [help.shareview.co.uk](https://help.shareview.co.uk) (from here you will be able to email your query securely).

- Change of address
- Lost share certificates or dividend cheques
- Dividend mandates
- Amalgamation of holdings

Forms for some of these matters can be downloaded from the registrars' website [www.shareview.co.uk](https://www.shareview.co.uk). Shareholders can easily access and maintain their shareholding online by registering at [www.shareview.co.uk](https://www.shareview.co.uk). To register, shareholders will require their shareholder reference number which was recently provided. This is the 11 digit number found on recent dividend correspondence.

## Share dealing service

For information on the share dealing service offered by Equiniti Limited, telephone 0345 603 7037 (+44 121 415 7065 if calling from outside the UK). Lines open 8.00am to 4.30pm (UK time), Monday to Friday excluding public holidays in England and Wales). Please either telephone Equiniti or look online at [www.shareview.co.uk](https://www.shareview.co.uk) for up-to-date commission rates.

## Dividend reinvestment plan (DRIP)

Equiniti's Dividend Re-investment Plan offers a convenient way for shareholders to build up their shareholding by using dividend payments to purchase additional shares. The plan is provided by Equiniti Financial Services Limited, part of Equiniti Group, which is authorised and regulated by the Financial Conduct Authority.

For more information and an application pack please call 0333 207 5951 (+44 121 415 0804 if calling from outside the UK). Lines open 8.30am to 5.30pm (UK time), Monday to Friday excluding public holidays in England and Wales. Alternatively go to [shareview.co.uk/info/drip](https://shareview.co.uk/info/drip).

It is important to remember that the value of shares and dividend payments can fall as well as rise and you may not recover the amount of money that you invest. Past performance should not be seen as indicative of future performance.

## Overseas shareholders

Equiniti provides a service to overseas shareholders that will convert sterling dividends into local currency at a competitive rate. Dividend payments will then be made directly into your local bank account. For more information log on to [www.shareview.co.uk/info/ops](https://www.shareview.co.uk/info/ops) where you will find the answer to any queries you have, as well as the full terms and conditions of the service. Alternatively please call 0333 207 5951 (+44 121 415 0804 if calling from outside the UK). Lines open 08.30am to 5.30pm (UK time), Monday to Friday excluding public holidays in England and Wales.

## Duplicate share register accounts

If you are receiving more than one copy of our report, it may be that your shares are registered in two or more accounts on our register of members. If that was not your intention you might consider merging them into one single entry. Please contact Equiniti, who will be pleased to carry out your instructions.

# Shareholder enquiries continued

## Shareholder analysis

Analysis of share register as at 19 February 2019:

<b>Holding range</b>	<b>Number of shareholders</b>	<b>%</b>	<b>Number of shares</b>	<b>%</b>
1 to 1,000	861	43.1	358,576	0.2
1,001 to 10,000	743	37.2	2,291,930	1.2
10,001 to 100,000	217	10.9	8,054,502	4.2
100,001 to 500,000	96	4.8	23,681,760	12.4
500,001 and over	79	4.0	157,069,404	82.0
	1,996	100.0	191,456,172	100.0

<b>Type of shareholders</b>	<b>% of shareholders</b>	<b>% of total shares</b>
Directors' interests	0.1	0.1
Major institutional and corporate holdings	34.6	98.3
Other shareholdings	65.3	1.6
	100.0	100.0

As at 25 February 2019 the following voting rights in the Company had been notified in accordance with the Disclosure and Transparency Rules.

<b>Name of shareholders</b>	<b>Number of shares</b>	<b>%</b>
Aberdeen Standard Investments	19,289,728	10.1
Merian Global Investors (UK) Limited	13,886,391	7.3
Franklin Templeton Fund Management Limited	10,062,315	5.3
BlackRock Investments Management (UK) Ltd	9,889,340	5.2
Norges Bank Investment Management	7,216,481	3.8
AXA Investment Managers UK Ltd	7,018,428	3.7
Dimensional Fund Advisors, LP	7,004,171	3.7
The Vanguard Group, Inc.	6,323,859	3.3
Schroder Investment Management Ltd	6,312,497	3.3
Baillie Gifford & Co.	5,979,970	3.1



# Company information

## Advisers

### Auditor

Deloitte LLP

### Principal bankers

HSBC Bank plc, Barclays Bank PLC, The Royal Bank of Scotland plc, Svenska Handelsbanken AB, UniCredit Bank AG, ING Bank NV, Wells Fargo Bank, NA and KBC Bank NV.

### Solicitors

Eversheds Sutherland (International) LLP, Herbert Smith Freehills LLP and DLA Piper UK LLP.

## Financial calendar

Annual General Meeting

Final dividend for 2018

Interim results for 2019

Interim dividend for 2019

Results for 2019

24 May 2019

7 June 2019

July 2019

November 2019

February 2020



**Cover image**

This magnification shows an aluminum alloy section following solution heat treatment, quenching and ageing. Many wrought and cast aluminum alloys can be strengthened by these classical heat treatment processes, by producing precipitates of the alloying material within the metal structure, thus optimising their mechanical properties. These processes can also be used to strengthen nickel alloys and stainless steels.

[www.bodycote.com](http://www.bodycote.com)

 For the online version of this report go to  
[bodycote.annualreport2018.com](http://bodycote.annualreport2018.com)

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