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# Diploma PLC

Company Number: 3899848

## Annual Report and Accounts For the year ended 30 September 2018

THESE PARENT COMPANY ACCOUNTS  
FORM PART OF THE PACKAGE OF  
ACCOUNTS FOR SUBSIDIARY COMPANY  
EDCO SEAL AND SUPPLY LIMITED (REGISTERED  
IN ENGLAND & WALES, NO. 5653605).

TUESDAY



\*R88D9I2P\*  
RM 25/06/2019 #1  
COMPANIES HOUSE

# DIPLOMA PLC IS AN INTERNATIONAL GROUP OF BUSINESSES SUPPLYING SPECIALISED TECHNICAL PRODUCTS AND SERVICES

WE OPERATE GLOBALLY IN  
THREE DISTINCT SECTORS

## LIFE SCIENCES

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Suppliers of consumables, instrumentation and related services to the healthcare and environmental industries.

For more information  
See pages 14-17

## SEALS

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Suppliers of seals, gaskets, filters, cylinders, components and kits for heavy mobile machinery and specialised industrial equipment.

For more information  
See pages 18-21

## CONTROLS

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Suppliers of specialised wiring, cable, connectors, fasteners and control devices for technically demanding applications.

For more information  
See pages 22-25

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## FINANCIAL HIGHLIGHTS

FOR THE YEAR ENDED 30 SEPTEMBER 2018

# STRONG RESULTS WITH DOUBLE-DIGIT EARNINGS GROWTH

STRATEGIC REPORT

GOVERNANCE

FINANCIAL STATEMENTS

<p>↑</p> <p>REVENUE</p> <p><b>£485.1m</b></p> <p>2017: £451.9m</p> <p><b>+7%</b></p>	<p>↑</p> <p>STATUTORY OPERATING PROFIT</p> <p><b>£73.2m</b></p> <p>2017: £68.5m</p> <p><b>+7%</b></p>	<p>↑</p> <p>STATUTORY PROFIT BEFORE TAX</p> <p><b>£72.7m</b></p> <p>2017: £66.8m</p> <p><b>+9%</b></p>
<p>↑</p> <p>ADJUSTED OPERATING PROFIT<sup>1</sup></p> <p><b>£84.9m</b></p> <p>2017: £78.2m</p> <p><b>+9%</b></p>	<p>↑</p> <p>ADJUSTED OPERATING MARGIN<sup>1</sup></p> <p><b>17.5%</b></p> <p>2017: 17.3%</p> <p><b>+20bps</b></p>	<p>↑</p> <p>ADJUSTED PROFIT BEFORE TAX<sup>1,2</sup></p> <p><b>£84.8m</b></p> <p>2017: £77.5m</p> <p><b>+9%</b></p>
<p>↑</p> <p>FREE CASH FLOW<sup>3</sup></p> <p><b>£60.5m</b></p> <p>2017: £55.7m</p> <p><b>+9%</b></p>	<p>↑</p> <p>ACQUISITION SPEND</p> <p><b>£20.4m</b></p> <p>2017: £20.1m</p>	<p>↑</p> <p>ROATCE</p> <p><b>24.5%</b></p> <p>2017: 24.0%</p> <p><b>+50bps</b></p>

	2018 pence		2017 pence
Adjusted earnings per share <sup>1,2</sup>	56.4	+13%	49.8
Basic earnings per share	47.5	+13%	42.0
Total dividend per share	25.5	+11%	23.0
Free cash flow per share <sup>3</sup>	53.5	+9%	49.3

1 Before acquisition related charges and Chief Executive Officer transition costs  
2 Before fair value remeasurements  
3 Before cash payments on acquisitions and dividends

Diploma PLC uses alternative performance measures as key financial indicators to assess the underlying performance of the Group. These include adjusted operating profit, adjusted profit before tax, adjusted earnings per share, free cash flow, trading capital employed and return on adjusted trading capital employed ("ROATCE"). All references in this Annual Report & Accounts to "underlying" revenues or operating profits refer to reported results on a constant currency basis and before any contributions from acquired or disposed businesses. The narrative in the Annual Report & Accounts is based on these alternative measures and an explanation is set out in note 2 and 3 to the consolidated financial statements.

## CHAIRMAN'S STATEMENT

JOHN NICHOLAS CHAIRMAN

# RESILIENT BUSINESS, CONSISTENT DELIVERY, STRONG RESULTS

### PRINCIPAL CORPORATE OBJECTIVES

ACHIEVE DOUBLE-DIGIT  
GROWTH IN ADJUSTED EPS  
OVER THE BUSINESS CYCLE

—  
GENERATE TSR GROWTH  
IN THE UPPER QUARTILE  
OF THE FTSE 250

—  
DELIVER PROGRESSIVE  
DIVIDEND GROWTH  
WITH TWO TIMES  
DIVIDEND COVER

Diploma's trading performance in 2018 was, once again, very strong. The Group delivered another year of double-digit growth in adjusted earnings per share and generated free cash flow of over £60m. The results demonstrate the resilience of the Group's businesses and the consistent delivery against the Group's strategy that have allowed Diploma to build a long track record of strong financial performance despite the vagaries of the macroeconomic environment during any period.

During the year the Board appointed a new Chief Executive Officer ("CEO") to succeed Bruce Thompson who retired from the Board after leading the Group for over 20 years. However, in August it was announced that Richard Ingram stepped down from his role as CEO and that I had agreed to take over as interim Executive Chairman until a new CEO is appointed. This process is under way and the Board is confident that we will find the right CEO to lead the Group to continued success. Over the course of this year, I have been consistently impressed by the capability and commitment of

the Group's senior management team and I am grateful for their continued support and hard work during this period. My particular thanks are extended to our Group Finance Director, Nigel Lingwood, for the strength and leadership he has demonstrated throughout the year.

The Board has reviewed and reconfirmed its support for the Group's existing strategy that we believe continues to have excellent potential to create shareholder value in the years ahead. In addition to the underlying growth achieved this year, two acquisitions were completed during the year and a further small acquisition was also completed shortly after the year end.

#### RESULTS

Group revenues increased in 2018 by 7% to £485.1m (2017: £451.9m), despite a currency headwind of 3% from translating the results of the overseas businesses, following a small appreciation in UK sterling this year. After adjusting for the contribution from acquisitions completed both this year and last year, net of a small disposal this year and for these

currency effects on translation, Group revenues also increased by 7% on an underlying basis. The Seals businesses delivered strong underlying revenue growth of 10% and both the Life Sciences and Controls businesses reported a 5% growth in underlying revenues.

Adjusted operating profit increased by 9% to £84.9m (2017: £78.2m) reflecting the strong growth in revenues and a modest increase of 20bps in adjusted operating margins to 17.5% (2017: 17.3%). Adjusted profit before tax also increased by 9% to £84.8m (2017: £77.5m) and adjusted earnings per share ("EPS") increased by 13% to 56.4p (2017: 49.8p), reflecting the benefit from the reduction in the US Federal corporate income tax rate during the year.

On a statutory basis, the Group's operating profit was 7% ahead of last year at £73.2m (2017: £68.5m) after £9.6m (2017: £9.7m) of acquisition related charges, largely comprising amortisation of acquired intangible assets and one-off charges of £2.1m with respect to the CEO change in the year. Statutory profit

## // THE GROUP HAS MAINTAINED ITS LONG TRACK RECORD OF CONSISTENT DELIVERY AGAINST ITS KEY PERFORMANCE METRICS //

before tax increased by 9% to £72.7m (2017: £66.8m) and statutory EPS was 13% up on last year at 47.5p (2017: 42.0p).

The Group's free cash flow remained robust at £60.5m (2017: £55.7m), which included £4.0m from the sale of a small non-core US gasket business. The outflow of cash to support working capital increased again this year by £5.1m (2017: £4.0m) reflecting the much stronger trading environment across the Group. Capital expenditure increased this year to £6.6m (2017: £3.3m) with investment focused on new facilities and IT infrastructure and a large investment by the Healthcare businesses in field equipment in support of customer contracts.

As indicated in last year's Annual Report, the environment to complete acquisitions continued to be challenging as vendors postponed their exit plans in the face of the continuing favourable macroeconomic conditions. The Group invested £20.4m (2017: £20.1m) in acquisitions and there were tentative signs towards the end of the year that this environment was easing. The pipeline of acquisition opportunities remains healthy and we are confident that good quality businesses in our acquisition pipeline will be brought to market by their vendors.

The Group's balance sheet remains robust with cash funds at 30 September 2018 of £36.0m (2017: £22.3m), after investing £20.4m in acquisitions and making distributions to shareholders of £26.8m (2017: £23.5m). The Group also has unutilised committed bank facilities of £30m with an accordion option to extend these facilities up to £60m.

### DIVIDENDS

The combination of strong results and free cash flow, supported by a robust balance sheet has led the Board to recommend an increase in the final dividend of 11% to 17.8p per share (2017: 16.0p). Subject to shareholder approval at the Annual General Meeting ("AGM"), this dividend will be paid on 23 January 2019 to shareholders on the register at 30 November 2018.

The total dividend per share for the year will be 25.5p (2017: 23.0p), which represents an 11% increase on 2017, with the level of dividend cover remaining unchanged at 2.2 times on an adjusted EPS basis.

### GOVERNANCE

During the year, we completed an external evaluation of the Board. The results of the review were discussed by the Board and an action plan to implement suggested improvements has been prepared. The review included an in-depth analysis of the CEO recruitment process with specific lessons to learn for the new search. The Nomination and Remuneration Committees have been focused during the latter part of the year on the leadership change and search for a new CEO. The Audit Committee has overseen the transition of the audit to the new auditor, PricewaterhouseCoopers LLP.

### EMPLOYEES

We continue to foster an entrepreneurial culture that encourages our employees to take responsibility for their own businesses. I would like to record my thanks to all our employees whose hard work and commitment has again been a driving force behind the Group's performance and the achievement of another year of strong financial results.

### OUTLOOK

Diploma has a strong and resilient business model with a broad geographic spread of businesses supported by a robust balance sheet and consistently strong free cash flow. This model has delivered another strong result this year with double-digit growth in earnings per share, benefiting from favourable trading conditions in most of its major markets.

Despite the global macroeconomic uncertainty, the Board remains confident that the Group will continue to make further progress in the coming year from a combination of steady "GDP plus" underlying growth and from the Group's proven value-enhancing acquisition programme.

ADJUSTED EPS GROWTH (PENCE)

**+13% p.a.<sup>1</sup>**

TSR GROWTH (TSR INDEX 2008 = 100)

**+29% p.a.<sup>1</sup>**

DIVIDEND GROWTH (PENCE)

**+13% p.a.<sup>1</sup>**

<sup>1</sup> Ten-year compound.

## GROUP AT A GLANCE

# WELL DIVERSIFIED BY GEOGRAPHY AND BUSINESS AREA

### NORTH AMERICAN REVENUES (BY DESTINATION) BY SECTOR

GROUP REVENUE

40%

23% US 17% CANADA

### EUROPEAN REVENUES (BY DESTINATION) BY SECTOR

GROUP REVENUE

48%

23% UK 25% EUROPE

### REST OF WORLD REVENUES (BY DESTINATION) BY SECTOR

GROUP REVENUE

12%

### LIFE SCIENCES

See pages 14-17



### SEALS

See pages 18-21



### CONTROLS

See pages 22-25



#### Healthcare (85% of revenues)

Clinical diagnostic instrumentation, consumables and services supplied to hospital pathology and life sciences laboratories for the testing of blood, tissue and other samples.

Surgical medical devices and related consumables and services supplied to hospital operating rooms, GI/Endoscopy suites and clinics.

#### Environmental (15% of revenues)

Environmental analysers, containment enclosures and emissions monitoring systems.

#### GROUP REVENUE

28%

#### EMPLOYEES

426

#### PRIMARY GROWTH DRIVERS

Public and private healthcare spending

Population ageing and increasing life expectancy

Health & Safety and Environmental regulation

#### North America - Aftermarket (31% of revenues)

Next day delivery of seals, sealing products and cylinder components for the repair of heavy mobile machinery.

#### North America - Industrial OEM (29% of revenues)

Sealing products, custom moulded and machined parts supplied to manufacturers of specialised industrial equipment.

#### International (40% of revenues)

Sealing products and filters supplied outside North America to Aftermarket and Industrial OEM customers as well as to Maintenance, Repair and Overhaul ("MRO") operations.

#### GROUP REVENUE

43%

#### EMPLOYEES

821

#### PRIMARY GROWTH DRIVERS

General economic growth

Activity and spending levels in Heavy Construction and Infrastructure

Growth in industrial production

MRO expenditure in Mining and process industries

#### Interconnect (59% of revenues)

Wiring, cable, harness components and cable accessories used in specialised technical applications in Aerospace, Defence, Motorsport, Energy, Medical, Rail and Industrial.

#### Specialty Fasteners (21% of revenues)

Specialty aerospace-quality fasteners supplied to Civil Aerospace, Motorsport, Industrial and Defence markets.

#### Fluid Controls (20% of revenues)

Temperature, pressure and fluid control products used in Food & Beverage and Catering industries.

#### GROUP REVENUE

29%

#### EMPLOYEES

542

#### PRIMARY GROWTH DRIVERS

General growth in the industrial economy

Activity and spending levels in Aerospace, Defence, Motorsport, Energy, Medical and Rail

Equipment installation & maintenance in Food & Beverage and Catering

## OUR YEAR IN REVIEW

# ANOTHER YEAR OF ROBUST GROWTH IN REVENUE AND EARNINGS

**“THE GROUP’S STRATEGY, CONSISTENTLY  
APPLIED, DELIVERS STRONG GROWTH  
IN EARNINGS AND SHAREHOLDER VALUE”**

### FINANCIAL PERFORMANCE

In 2018, the Group delivered another year of robust growth in revenue and earnings benefiting from strong industrial economies in the US and Europe and from the reduction in the US Federal corporate income tax rate.

The Group’s reported revenues increased by 7%, with currency headwinds decreasing revenues by 3% and acquisitions, net of a small disposal this year, contributing 3% to revenue growth. On an underlying basis, after adjusting for acquisitions, the disposal and for the currency effects on translation, Group revenues increased by 7%.

The Group’s adjusted operating margins improved by 20bps to 17.5%, compared with 17.3% in the prior year and the first half of the current year. Gross margins remained unchanged from last year, despite pressures on supply chains in most Sectors leading to increases in product costs and other margin support costs. These pressures were mitigated during the second half of the year as selective price increases began to take effect and with increased availability of inventory. Adjusted operating costs as a percentage of revenue have reduced by 20bps with improved operating leverage from the increase in revenues and generally tight control of operating costs.

Working capital as a percentage of revenue was managed down through the second half of the year to 15.1%. The Group’s free cash flow increased by 9% to £60.5m, reflecting very strong cash generation in the second half of the year and boosted by proceeds of £4.0m from the disposal of a small non-core US business.

### SECTOR PERFORMANCE

In **Life Sciences**, underlying revenues increased by 5% after adjusting for currency movements and the prior year acquisition of Abacus ALS. The Healthcare businesses benefited from strong diagnostic consumable revenues and the introduction of new premium Surgical and Endoscopy products. The Environmental businesses had a mixed year with stronger revenues in Germany, offset by reduced UK revenues because of delays in placement of orders. Both Environmental businesses continued to benefit from stronger service revenues.

In **Seals**, underlying revenues increased by 10% after adjusting for currency movements, the prior year acquisitions of PSP and Edco and the disposal of the small non-core Bulldog business this year. In North America, both the Aftermarket and Industrial OEM business benefited from a buoyant US industrial economy. In the International Seals businesses, a strong improvement in industrial activity in the second half of the year provided good growth in European revenues. Solid growth in Australian revenues was more than offset by much weaker trading with a major customer in New Caledonia.

In **Controls**, underlying revenues increased by 5% after adjusting for currency movements and the acquisitions this year of FS Cables and Coast. The Interconnect revenues benefited from both broadening its customer base deeper into Europe and from stronger industrial markets. The Specialty Fasteners business also increased revenues from broadening its range of customers in the Civil Aerospace sector. The Fluid Controls businesses reported lower revenues reflecting

the decision to focus on higher margin business and from the absence of a large one-off project delivered last year.

### ACQUISITIONS AND DISPOSALS

Over the last five years, a total of ca. £128m has been invested in acquisitions and ca. £6m has been realised from divesting businesses.

During 2018, the acquisition spend was £20.4m of which £16.9m was invested in the acquisition of FS Cables, a supplier of specialist cable products to a range of industries and based in St Albans, UK. FS Cables fits well within the Controls Sector alongside Cablecraft, which was acquired in 2016 and provides growth opportunities through cross-selling to new and existing customers. The small non-core US business, Bulldog, was sold during 2018 for cash proceeds of £4.0m.

In addition, the Group completed two smaller bolt-on acquisitions in the Controls Sector: Coast, a small specialty fastener distributor based in California, US was acquired in October 2017 and Gremtek, a supplier of protective own-brand sleeving products, based in France was acquired after the year end in October 2018.



**STRONG EXECUTIVE MANAGEMENT**

The Executive Management Committee ("EMC") comprises the Executive Directors along with the Executive managers who are responsible for the major business clusters and key Group functions. The EMC members are a combination of internally developed senior managers and experienced senior managers who have been recruited externally.

The EMC has been strengthened this year with experienced senior management who will take responsibility for overseeing and coordinating additional Group functions, including IT and ERP projects carried out across the Group. A HR senior manager is also being recruited and will join the EMC in the new financial year.

The EMC provides the opportunity for members to broaden their perspective of the Group's activities in order to reinforce the key elements of the Group's culture and to identify best practices that are transferable across the Group. The EMC meets quarterly through a combination of full group meetings in London and sub-group meetings held in the major business locations.

During this year, the EMC has demonstrated its strength by providing a significant level of stability and support to the businesses in a period of uncertainty caused by the change in CEO. This has contributed to the strong results reported this year.

## OUR BUSINESS MODEL

# MAKING US ESSENTIAL TO OUR CUSTOMERS

OUR BUSINESS MODEL IS BUILT ON THE  
THREE "ESSENTIALS" – PRODUCTS,  
SOLUTIONS AND VALUES

WHAT WE PUT IN

ESSENTIAL  
PRODUCTS



Our businesses focus on supplying essential products and services funded by customers' operating rather than capital budgets and supplied across a range of specialised industry segments.

The majority of the Group's revenues are generated from consumable products. In many cases, the products will be used in repair and maintenance applications and refurbishment and upgrade programmes, rather than supplied to original equipment manufacturers.

ESSENTIAL  
SOLUTIONS



Our businesses design their individual business models to provide solutions that closely meet the requirements of their customers:

Highly responsive customer service, such as the next day delivery from stock of essential, but low value items.

Deep technical support, where we work closely with our customers in designing our products into their specific applications.

Added value services which, if we did not provide these services, customers would have to pay others to provide or would require investment in additional resources of their own.

ESSENTIAL  
VALUES



We encourage an entrepreneurial culture across our businesses, through a decentralised management structure.

We want our managers to feel that they have the freedom to run their own businesses, while being able to draw upon the support and resources of a larger group where this is beneficial.

Within our businesses we have strong, self-standing management teams who are committed to and rewarded according to the success of their businesses.

HOW WE'VE MADE PROGRESS



Performance is measured by the underlying growth in revenue, after adjusting for currency and acquisitions/disposals:

This year, the underlying growth has been 7%.

Over five years, the average underlying growth has been 5% p.a.

For more information  
See page 13



Performance is measured by the level and stability over time of gross and operating margins:

Gross margins have remained broadly stable over many years, excluding shorter term currency effects.

This year, adjusted operating margin improved 20bps to 17.5%.

Over five years, the average adjusted operating margin has been 17.7%.

For more information  
See page 13



Performance is more difficult to measure directly, but non-financial KPIs can give an indication of organisational stability and health. Over the last five years:

Average length of service for all employees has been ca. 7 years (ca. 11 years for the senior management cadre).

Number of working days lost to sickness has consistently been ca. 1% a year.

For more information  
See page 13

WHAT WE GET OUT

RECURRING INCOME AND STABLE  
REVENUE GROWTH

Our focus on essential products and services contributes to the Group's record of stable revenue growth over the business cycle.

Our businesses target "GDP plus" levels of underlying revenue growth over the economic cycle, with higher growth rates achieved at the Group level, through carefully selected value enhancing acquisitions.

SUSTAINABLE AND  
ATTRACTIVE MARGINS

By supplying solutions, not just products, we build strong long term relationships with our customers and suppliers, supporting sustainable and attractive margins.

Our businesses achieve sustainable and attractive gross margins by offering strongly differentiated products and customer focused solutions within specialised market segments. By running efficient operations, these gross margins are converted into healthy operating margins.

AGILITY AND  
RESPONSIVENESS

Our decentralised organisational model ensures that decisions are made close to the customer and that the businesses are agile and responsive to changes in the market and the competitive environment.

Agility and responsiveness in the businesses ensure close management of operating costs and working capital and deliver strong free cash flow.

## GROWTH STRATEGY

# COMPOUNDING GROWTH THROUGH ACQUISITIONS

GROWTH IS ACCELERATED BY INVESTING  
IN VALUE ENHANCING ACQUISITIONS

WHAT WE PUT IN

ACQUIRE



Clear business criteria have been established to guide the Group's acquisition programme:

- fit with the Group's business model;
- marketing led with strong customer relationships;
- secure supply of high quality, differentiated products; and
- capable management.

The principal financial criteria are:

- Track record of stable, profitable growth and cash generation.
- Exceed post-tax IRR threshold of 13% to ensure 20%+ pre-tax return on investment.

BUILD



The acquisitions we make are of businesses that are already successful and with a good track record. However, these businesses have typically reached the point where additional resources are needed to take them to the next level of growth.

Working with management, we provide the investment required to build a solid foundation to allow the business to move to a new level of growth. The investment we make in new acquisitions will normally be in new facilities and IT systems, increased but better managed working capital and additional management resource.

GROW



Once the acquisition is integrated into the Group, with a solid platform established, the focus is on delivering stable, profitable growth.

The results of the Acquire, Build, Grow strategy can be seen in the improving revenue growth and operating margins post-acquisition.

WHAT WE GET OUT



Acquisitions give entry into new but related markets and thereby extend the reach of the existing businesses and bring new growth opportunities.

The Group applies a consistent level of effort and resources to identifying and developing acquisition opportunities. However, the output in terms of acquisitions completed, ebbs and flows depending on the acquisition environment.

To achieve the Group's objective of strong double-digit growth, acquisition spend of at least £30m p.a. is targeted.



Except in the case of smaller bolt-on acquisitions, the acquired companies maintain their distinct sales and marketing identity and strong independent management teams.

Where there are opportunities for synergies with other Group businesses, these are managed in larger business clusters. Synergies typically include:

- Cross-selling between the businesses
- Joint purchasing between the businesses
- Shared operational infrastructure and shared back-office functions



By the third year post-acquisition, underlying revenue growth for the acquired businesses is typically higher than the Group average and operating margins have improved by 200-300bps on average.

These improvements in financial performance ensure that the Group creates value through its acquisition programme and maintains ROATCE above the 20% threshold.



HOW WE'VE MADE PROGRESS

COAST

In October 2017, Clarendon Specialty Fasteners acquired the business and assets of Coast Fabrication Inc, a small specialty fastener distributor based in California, US. Coast has a strong reputation in US Motorsport which complements Clarendon's strong Motorsport presence in Europe. Coast also provides a US base to expand Clarendon's existing aircraft interiors business in this large market and allows Clarendon to access the major US fasteners suppliers. Revenues of Clarendon, including Coast, grew by 25% in 2018.

For more information  
See pages 22-25

ABACUS dx

Since being acquired in 2017, the business has been integrated with our existing DS business and has invested in expanded shared service facilities in Melbourne, Sydney and Brisbane, whilst cross-training technical and applications support personnel at both the global supplier and local level. As a result Abacus dx was able to sell and service over 90 diagnostic instrument placements in 2018 and benefit from the associated pull-through in consumable sales. Revenues of Abacus dx grew by 9% on a like-for-like basis in 2018.

For more information  
See pages 14-17

US INDUSTRIAL OEM SEALS

After clustering these businesses under a single senior management team, an ERP system was implemented in 2018 to replace a number of legacy systems. This will allow the management team to consolidate back-office processes to improve visibility of customer activity, inventory and supplier information, and finance. Each location will continue to maintain its own distinct identity, but the ERP system will allow the business to service customers using shared knowledge and products that will increase the value to the customer. Revenues of this business cluster grew by 13% in 2018.

For more information  
See pages 18-21

## STRATEGIC PRIORITIES AND KPIs

### STRATEGIC PRIORITY

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#### GDP+ UNDERLYING REVENUE GROWTH

We focus on essential products and services, funded by customers' operating rather than capital budgets, giving resilience to revenues.



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#### ATTRACTIVE MARGINS

Our attractive operating margins are sustained through the quality of customer service, the depth of technical support and value adding activities.



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#### AGILE AND RESPONSIVE ORGANISATION

We encourage an entrepreneurial culture in our businesses through our decentralised organisation.



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#### ACQUISITIONS TO ACCELERATE GROWTH

Carefully selected, value enhancing acquisitions accelerate the underlying growth and take us into related strategic markets.



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#### STRONG CASH FLOW

An ungeared balance sheet and strong cash flow fund our growth strategy while providing healthy and growing dividends.



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#### VALUE CREATION

We aim to create value by consistently exceeding 20% ROATCE.



KEY PERFORMANCE INDICATORS

REVENUE GROWTH (£M)

+11%

FIVE-YEAR COMPOUND

UNDERLYING REVENUE GROWTH (%)

+5%

FIVE-YEAR AVERAGE

ADJUSTED OPERATING MARGIN (%)

18%

FIVE-YEAR AVERAGE

ADJUSTED OPERATING MARGIN (ΔBPS)

Improvement in adjusted  
operating margin of  
acquired businesses three  
years after acquisition

+200–  
300bps

LENGTH OF SERVICE (YEARS)

6.6 years

FIVE-YEAR AVERAGE

AVERAGE WORKING DAYS LOST  
TO SICKNESS (%)

1%

FIVE-YEAR AVERAGE

ACQUISITION SPEND (£M)

£25.5m

FIVE-YEAR AVERAGE

REVENUE FROM ACQUISITIONS (% OF TOTAL)

15%

FIVE-YEAR AVERAGE

FREE CASH FLOW (£M)

£50.7m

FIVE-YEAR AVERAGE

WORKING CAPITAL (% OF REVENUE)

16%

FIVE-YEAR AVERAGE

ROATCE (%)

24%

FIVE-YEAR AVERAGE

## LIFE SCIENCES

THE LIFE SCIENCES  
SECTOR BUSINESSES  
SUPPLY A RANGE  
OF CONSUMABLES,  
INSTRUMENTATION  
AND RELATED SERVICES  
TO THE HEALTHCARE  
AND ENVIRONMENTAL  
INDUSTRIES

### PRINCIPAL SEGMENTS

#### GEOGRAPHY

50% Canada  
26% Europe  
24% Australasia

#### CUSTOMERS

84% Clinical  
9% Utilities  
3% Chemical & Pharmaceutical  
2% Life Sciences Research  
2% Other Life Sciences

#### PRODUCTS

70% Consumables  
21% Instrumentation  
9% Service

#### HEALTHCARE

The Diploma Healthcare Group ("DHG") operates in three principal geographies - Canada, Australasia and Europe. In Canada, DHG supplies to the ca. 600 public hospitals across the country as well as to private clinics and pathology laboratories. Somagen Diagnostics ("Somagen") supplies a range of consumables and instruments used in the diagnostic testing of blood, tissue and other samples. It is also a leading supplier to the growing cancer screening and the assisted reproductive technology ("ART") markets. AMT/Vantage comprises the AMT Surgical and Vantage Endoscopy ("Vantage") divisions. AMT Surgical supplies specialised equipment and consumables for electrosurgery and minimally invasive ("MI") surgery use in hospital operating rooms. Vantage supplies endoscopes and related consumables, therapeutic devices and services to GI Endoscopy suites in hospitals and private clinics. Vantage is also expanding its portfolio into the Urology and Gynaecology surgical segments with rigid and flexible scopes and specialised instrument sets.

In Australia and New Zealand, DHG also supplies to hospitals, private clinics and pathology laboratories. In April 2017, DHG acquired Abacus ALS, a long established supplier of instrumentation and consumables to the Pathology and Life Sciences sectors. At the start of the current financial year, Abacus ALS was combined with Diagnostic Solutions to form Abacus dx, a market leading clinical diagnostics business supplying to both public and private laboratories. Big Green Surgical ("BGS") supplies a range of products to the Surgical Products sector. Abacus dx and BGS share several common suppliers with DHG's Canadian businesses.

In Europe, DHG operates through Technopath Distribution ("TPD"), an established supplier of products to the Biotechnology, Clinical Laboratory and Medical Device markets in Ireland and the

UK. Similar to the other DHG businesses, TPD focuses on specialised laboratory diagnostics and specialty medical device segments, again leveraging several common suppliers.

#### ENVIRONMENTAL

The a1-group is a supplier to Environmental testing laboratories and to Health & Safety engineers. The a1-envirosciences business, based in Germany, supplies a range of containment enclosures for potent powder handling. The a1-CBISS business, based in the UK, supplies equipment and services for the monitoring and control of environmental emissions, as well as a range of gas detection devices.

#### MARKET DRIVERS

The DHG businesses in Canada supply into areas of **Healthcare** that are predominantly public sector funded. Private sector funding, representing ca. 30% of Healthcare expenditure in Canada, is largely focused on areas where DHG does not participate, specifically dental, cosmetic, eye surgery and pharmaceuticals. The principal demand driver for DHG in Canada is therefore the sustainable level of Healthcare spending funded by the Canadian Government.

The Canadian Health Act ("the Act") ensures universal coverage for all insured persons for all medically necessary services provided by hospitals, physicians and other Healthcare providers. A growing, ageing and well educated population demands high standards of service delivery, helping to ensure ongoing growing demand.

The Provinces are responsible for the delivery of the Healthcare services, but the Federal Government partially controls delivery through Federal Provincial transfer payments, which represent the largest source of revenues for the Provinces. The relative stability and consistency in funding by each of the Provinces, guaranteed through the Act, ensures that the market remains well funded through the economic cycle and current expenditure of 10.4%

### PRINCIPAL OPERATIONS

#### Healthcare

Somagen Diagnostics	Edmonton, AB, Canada
AMT/Vantage	Kitchener, ON, Canada
Abacus dx	Brisbane, QLD & Melbourne, VIC, Australia
Big Green Surgical	Melbourne, VIC, Australia
Technopath Distribution	Ballina, Co. Tipperary, Ireland

#### Environmental

a1-CBISS	Tranmere, UK
a1-envirosciences	Düsseldorf, Germany



of GDP (11.5% including capital expenditure) places Canada in the top 20% of OECD countries.

Over many years, Healthcare expenditure has grown steadily with annual variations mostly dependent on the periodic additional tranches of funding provided by individual Provinces. In periods when the economy has been slower, Healthcare funding has still shown growth, albeit at reduced levels. In 2017, public Healthcare spending in Canada was ca. C\$170bn, with the largest category of expenditure (ca. C\$70bn) being in the hospital sector.

The Healthcare market in Australia shares with Canada many of the same attractive characteristics for specialised distribution. While privately funded Healthcare is more prevalent in areas such as surgery and laboratory testing, public sector Healthcare funding is still large and supported by a stable, resource based economy. As with Canada, Australia has a large geography to be covered, low population density and purchasing processes that vary by State. These characteristics necessarily demand a significant investment by manufacturers in technical sales and service resource, which makes the specialised local distribution model a very attractive mechanism for manufacturers to serve the local markets.

Since 2013, the Canadian and Australian economies have come under pressure from low oil prices and reduced demand for the countries' natural resources. This tougher economic environment has resulted in greater pressure on budgets throughout the Healthcare systems in both countries. In such periods, Healthcare funding is tightly constrained through targeted controls imposed on the number of laboratory tests and operating procedures as well as more rigorous tendering and Group procurement processes for expenditure on capital equipment. Even with such pressures, however, Healthcare funding has shown positive growth in total Healthcare expenditure of 3-4% and 4-6% respectively in Canada and Australia.

The principal market driver for the TPD business is Healthcare funding in the UK and Ireland, which totals ca. £215bn, representing ca. 10% of combined GDP. The UK accounts for ca. 90% of the total funding and ca. 80% is provided by public funding and 20% by private funding. Following the 2009 recession, annual growth in UK Healthcare expenditure has slowed to

Total current Healthcare expenditure<sup>1</sup> as a percentage of GDP

	2013	2014	2015	2016	2017
Canada	10.1%	10.0%	10.4%	10.5%	10.4%
Australia	8.8%	9.1%	9.3%	9.3%	9.1%
Ireland	10.3%	9.7%	7.4%	7.4%	7.1%
UK	9.8%	9.7%	9.8%	9.8%	9.7%

Source: OECD

<sup>1</sup> Excluding capital expenditure.

low single-digit levels, compared with average growth of 8% p.a. over the previous decade. In Ireland, Healthcare expenditure saw reductions year-on-year in 2010 and 2011, since then growth has resumed at low single-digit levels.

The a1-group supplies to customers in the Environmental industry in the UK, Germany and France. The market demand is largely driven by **Environmental** and Health & Safety regulations and growth in recent years has been driven by the need

to be compliant with a range of EU regulations. Since market demand is driven by regulation, this ensures reasonably steady demand for essential consumable products and services, though customers may defer capital expenditure during significant downturns in the economy.

## LIFE SCIENCES

### HIGHLIGHTS FROM THE YEAR

- Sector revenue growth of 7%; underlying growth of 5% after adjusting for currency and an acquisition completed last year
- In Canada, DHG underlying revenues increased by 8% with strong consumable revenues from its leading products; the Surgical and Endoscopy products lines at the Vantage business reported strong revenues from the introduction of new premium products
- In Australia and New Zealand, underlying revenues increased by 4%; Abacus ALS acquired in April 2017 reported strong growth across its portfolio of products, which more than offset reduced revenues in the Surgical Products business following the acquisition of a key supplier by a large industry player
- TPD revenues were broadly flat in Ireland and the UK with new suppliers and product segments replacing suppliers moving to a direct supply model
- The Environmental businesses reported unchanged underlying revenues with strong revenue growth in Germany, offset by reduced revenues in the UK from delays in order placement

### SECTOR PERFORMANCE

Reported revenues of the Life Sciences Sector businesses increased by 7% to £134.7m (2017: £125.9m). The acquisition of Abacus ALS, acquired in April 2017, incrementally added £6.4m or 5% to Sector revenues, which was partly offset by a headwind of 3% from currency movements on translation of the results from overseas businesses to UK sterling. After adjusting for currency effects and this acquisition, underlying revenues increased by 5%.

Adjusted operating margins reduced by 80bps to 17.7% largely reflecting the investment made during the year developing opportunities for the new endoscopes introduced in Canada. DHG margins were also diluted from a full year contribution, together with one-off integration costs, of the combined diagnostic businesses in Australia and New Zealand and weaker revenues following a loss of a supplier in BGS. In addition, an increase in underlying costs in the Environmental businesses on unchanged revenues led to negative leverage. However gross margins improved reflecting a more favourable mix of revenues in both the Healthcare and Environmental business. Transactional currency pressures on the Healthcare margins remained subdued, but favourable currency hedges helped offset some volatility of the Canadian and Australian dollars relative to the US dollar and Euro during the second half of the year. Adjusted operating profits increased by 3% to £23.9m (2017: £23.3m).

The Life Sciences businesses invested £3.5m (2017: £2.0m) in new capital during the year of which £2.3m (2017: £1.6m) was spent on acquiring field equipment for both new placements in hospitals and laboratories and for loan equipment and demonstration models to support existing placements. The increase in spend on field equipment was largely driven by the launch of a new series of flexible endoscopes, together with the addition of a range of rigid endoscopes under a new supplier agreement. A further £0.6m was invested in completing the refurbishment of the AMT and Vantage office and service facilities in Kitchener and Markham, Canada and on a new facility for a1-CBIS in the UK. The balance of £0.6m was invested in warehouse equipment and on upgrading the IT infrastructure in both businesses. Free cash flow increased marginally to £17.3m (2017: £17.0m), reflecting reduced cash flows into working capital, offset by higher capital investment.

### Healthcare

The DHG businesses, which account for 85% of Life Sciences revenues, increased underlying revenues by 6% after adjusting for currency effects and the incremental revenue from the acquisition of Abacus ALS.

In Canada, underlying revenues increased by 8% against the background of continuing budget pressures throughout the Provincial healthcare systems, with Group Procurement Offices ("GPOs") continuing to restructure and amalgamate, both nationally and regionally.

Somagen's core Clinical Diagnostics business delivered an underlying increase of 2% in revenues, with steady growth in consumable and service revenues. Capital sales decreased reflecting the impact of laboratory centralisation and reduced spending after a "catch-up" in procurement last year, following the 2016 hospital spending freeze in some Provinces. Demand for diagnostic testing remained robust, particularly with a combination of strong growth and contract extensions for cancer screening tests and growth from new technology introduced in the areas of Autoimmunity. A long term contract was renewed with a major supplier and an additional supply agreement was gained during the year that will provide opportunities for Somagen in the Microbiology market. Somagen has also secured large Provincial contracts to provide colorectal cancer screening products and services that are expected to ramp up in the next financial year.

Revenue (£m)  
(Compound growth over five years)

+8%op.a.

### REVENUE

£134.7m

	2018	2017	
Revenue	£134.7m	£125.9m	+7%
Adjusted operating profit	£23.9m	£23.3m	+3%
Adjusted operating margin	17.7%	18.5%	-80bps
Free cash flow	£17.3m	£17.0m	+2%
ROATCE	19.1%	19.7%	-60bps

AMT and Vantage, the Surgical and Endoscopy businesses in Canada, delivered strong growth in revenues, primarily driven by the successful introduction and rebranding of a premium range of rigid and flexible endoscopes and surgical instrument sets in Vantage. These offer further growth potential in the Urology and Gynaecology segments of the surgical market. The introduction of a new series of endoscopes in early 2018 has also provided Vantage with opportunities to replace existing customer supply contracts in several Provinces. Strong growth was also achieved at AMT in the supply of specialised instruments used in laparoscopic and other minimally invasive surgical procedures. These growth initiatives have diversified the revenue streams across both the core surgical and GI businesses and mitigated the continuing pressures in the electrosurgery and smoke evacuation businesses, where pricing has now stabilised, albeit at lower levels. In October 2018, AMT secured a new five-year contract with a large GPO to provide electrosurgical and smoke evacuation products.

In Australia, Diagnostic Solutions has been integrated into Abacus ALS to form Abacus dx, a larger broader-based Clinical Diagnostics, Life Science and Patient Simulation business, supplying to both the public and private pathology laboratories and to research and educational establishments across Australasia. Abacus dx has delivered strong growth in revenues on a like-for-like basis, despite the continuing consolidation of testing within Clinical Diagnostics and expanded professional procurement in the fragmented Life Sciences market. Abacus dx is working closely with key suppliers to position itself strongly in response to the shift towards track based laboratory systems. BGS, the Surgical Products business, reported a reduction in revenues as it struggled with securing sales of new products introduced to replace electrosurgical products from a supplier that had been acquired by a larger industry player with its own channels to market. However strong growth from key suppliers of other Surgical Products helped mitigate some of the shortfall. In smoke evacuation, the implementation of nursing guidelines enforcing smoke evacuation compliance will drive longer term growth, but has also slowed evaluation and decision processes during the year.

The TPD business in Ireland and the UK reported revenues broadly flat in Euro terms, as it managed the transition of a number of suppliers who have moved from specialised distribution to a direct supply model. New suppliers have been secured that will help mitigate this transition, together with solid growth within the Clinical segment supplying clinical chemistry and serology control products. New suppliers and businesses providing agitators and separators used in the NHS Blood and Transplant service continued to diversify the breadth of the portfolio. The Biotechnology and Service segments also delivered good growth from strong capital sales, which reflected management's efforts to forge strong strategic partnerships with their diverse customer base both in Ireland and the UK. TPD is further broadening its service capability beyond diagnostic instrumentation and has established a new Surgical Products division to bring to market the electrosurgical and smoke evacuation products similar to those supplied by AMT and BGS in Canada and Australia, respectively.

#### Environmental

The a1-group of Environmental businesses in Europe, which account for 15% of Life Sciences revenues, saw revenues increase by 1% in UK sterling terms, but remained unchanged in constant currency terms.

The a1-envirosciences business based in Germany increased revenues by 7% in Euro terms driven by strong demand in Germany for high-end halogen analysers and increased sales of customised containment enclosures. The increasing environmental awareness and in particular, the anticipated regulations on toxic polyfluorinated compounds, found in a range of man-made products, is creating demand for these analysers in R&D and Environmental control. Health & Safety regulations continue to increase demand for customised containment enclosures for the safe weighing of hazardous materials. The business is also targeting investment in service personnel to support the larger installed base and demand from customers for faster response times. In addition, investment is being made in an IT based field service management system to enhance customer service and improve efficiency of its growing service team.

#### POTENTIAL FOR GROWTH

**Increase share of specialised segments of Healthcare markets in Canada, Australia and UK/Ireland**

**Leverage DHG product portfolio across existing businesses and extend into other medical disciplines**

**Pursue further Healthcare acquisition opportunities in Northern Europe and Asia-Pacific**

**Continue to develop product and geographic spread of Environmental businesses**

The a1-CBISS business based in the UK reported an 8% decrease in revenues reflecting significant delays during the year in order placement for continuous emissions monitoring systems ("CEMS"). However the opportunities in this sector remain encouraging with new Energy from Waste ("EFW") plants playing an important role in reducing landfill waste. Revenue from service contracts continues to grow as EFW plants supplied over the last 18 months become operational.

## SEALS

THE SEALS SECTOR BUSINESSES SUPPLY A RANGE OF SEALS, GASKETS, FILTERS, CYLINDERS, COMPONENTS AND KITS USED IN HEAVY MOBILE MACHINERY AND SPECIALISED INDUSTRIAL EQUIPMENT

### GEOGRAPHY

57%	North America
34%	Europe
9%	Rest of World

### CUSTOMERS

47%	Industrial OEMs
31%	Heavy Construction
18%	MRO & Other Industrial
3%	Dump & Refuse Trucks
1%	Logging & Agriculture

### PRODUCTS

38%	Seals & Seal Kits
18%	O-Rings
17%	Cylinder & Other
12%	Gaskets
11%	Filters
4%	Attachment Kits

### NORTH AMERICA

The **Aftermarket** businesses in North America supply seals and associated products to support a broad range of mobile machinery in applications that include Heavy Construction, Mining, Logging, Agriculture, Material Handling (lift trucks, fork lifts and dump trucks) and Refuse Collection. The products are generally supplied on a next day delivery basis and are used in the repair and maintenance of equipment after it has completed its initial warranty period or lease term or has been sold on the pre-used market. The main customers are machinery and cylinder repair shops, engine and transmission rebuilders and other heavy equipment parts distributors.

The **Industrial OEM** businesses in North America supply seals, gaskets, O-rings and custom moulded and machined parts to a range of Industrial OEM customers. The businesses work closely with customers to select the most appropriate seal design, material and manufacturer for the application, provide technical support and guidance during the product development process and deliver the logistics capabilities to supply from inventory to support small to medium sized production runs.

### INTERNATIONAL

The International Seals businesses outside North America supply a range of seals, gaskets, filters, custom moulded and machined parts and hydraulic cylinder components to both Aftermarket and Industrial OEM customers. The businesses also supply products to end users operating process plants within the Mining, Oil & Gas, Pharmaceutical, Chemical, Food and Energy sectors, where products are required to support Maintenance, Repair and Overhaul ("MRO") operations.

### MARKET DRIVERS - NORTH AMERICA

In the **Aftermarket** businesses in North America, the principal drivers are the general GDP growth, and activity and spending levels in the Heavy Construction and Infrastructure sectors. In 2018, the US economy is forecast to show annual GDP growth of 2.9% (2017: 2.3%) driven primarily by strong consumer spending, growth in business investments fuelled by major tax reforms and growth in exports. Although the imposition of tariffs has dampened its impact, export growth has been underpinned by a pick-up in the world economy. Total US Construction spend (including non-residential and infrastructure spend, as well as residential housing activity) has continued to rise through 2018.

Unit sales in the US of Construction Equipment (defined as heavy mobile equipment including excavators above 14 tonnes, crawler dozers and wheeled loaders) is important as a medium term indicator for Hercules' replacement hydraulic seals activities, as the new equipment will move out of the dealer warranty period in the following years. It is also a good short term indicator for the HKX attachment kit business. Demand for new equipment increased by ca. 9% in 2017. However, the demand for new equipment remains below 2015 levels as utilisation levels are high, the general mobile machinery population is relatively new, and contractors continue to opt for the rental model for their equipment needs.

In Canada, following a strong period of expansion, GDP growth has slowed to a more sustainable level, driven by smaller increases in public consumption and slower increases in exports resulting from an adjustment in automobile production and the outage of an Oil & Gas pipeline.

### PRINCIPAL OPERATIONS

#### North America (HFPG)

##### Aftermarket

Hercules US	Clearwater, FL, US
Hercules Canada	Barrie, ON & Montreal, QC, Canada
HKX	Monroe, WA, US

##### Industrial OEM

J Royal	Winston-Salem, NC & Tallahassee, AL, US; Shanghai, China
RT Dygert	Minneapolis, MN, Chicago, IL & Seattle, WA, US
All Seals	Lake Forest, CA, & Denver, CO, US

#### International

FPE Seals	Darlington & Aberdeen, UK; Breda, The Netherlands
Kentek	Helsinki, Finland; St. Petersburg, Russia; Riga, Latvia
M Seals	Espergaarde, Denmark; Halmstad, Sweden; Beijing, China; Gateshead & Leicester, UK
Kubo	Effretikon, Switzerland; Linz, Austria
WCIS	Perth & Brisbane, Australia; Noumea, New Caledonia

In 2018, a gradual restoration of oil pipeline capacity and strong US growth is forecast to result in robust GDP growth of 2.1%.

In general, the economic conditions in the South and Central American economies served by the North American Aftermarket businesses continue to be challenging but are showing signs of improvement with private consumption, exports and earthquake related reconstruction activities expected to have a positive impact.

For the **Industrial OEM Seals** businesses in North America, the principal market driver is the growth rate in the general industrial economy. US industrial production declined through 2015 and 2016 but, having achieved strong growth in 2017 and 2018, has now risen back above 2014 levels. Increases in Mining output supported by substantial gains in the Oil & Gas segment and continued strength in the general Manufacturing segment have been the primary drivers of recent growth.

#### MARKET DRIVERS - INTERNATIONAL

The International Seals businesses operate in a range of countries and diverse market sectors and each has its own specific market drivers. The most relevant market drivers and indicators are therefore the general GDP growth and Industrial sector performance for the major geographies in which the businesses operate.

In the UK, economic growth is forecast to be marginally higher in 2018 at the modest level of ca. 1.6% (2017: 1.8%), with stronger export growth offset by uncertainties over the outcome of Brexit negotiations and reduced levels of investment. The UK Construction sector, which drives the Aftermarket business, had been steadily growing since mid-2012 until growth slowed in 2017. Construction output contracted in the first quarter of 2018 but began to recover through the year. However, the environment remains highly uncertain with new orders at a low level.

In the Nordic region, all countries are forecast to show positive GDP growth in 2018. Average growth across the region is forecast to be ca. 2.4% (2017: 2.3%).

In Switzerland, after years of subdued growth, the manufacturing sector gained momentum in 2017 as exporters benefited from the depreciation of the Swiss franc against the Euro making exports of Swiss Industrial products more attractive. GDP growth is forecast to increase to ca. 2.3% in 2018 (2017: 1.1%), recovering to levels of growth similar to those achieved prior to the decoupling of the Swiss franc from the Euro.

#### GDP growth in principal International Seals territories

Real GDP growth	2014	2015	2016	2017	2018
UK	+3.1%	+2.3%	+1.9%	+1.8%	+1.6%
Nordic region	+1.7%	+2.5%	+2.3%	2.3%	+2.4%
Switzerland	+2.5%	+1.2%	+1.4%	+1.1%	+2.3%
Russia	+0.7%	-2.5%	-0.2%	+1.6%	+1.7%
Australia	+2.6%	+2.5%	+2.6%	+2.3%	+3.0%

Source: IMF and Nordic Statistics

In Russia, the impact of low oil prices and EU and US sanctions continues to hinder economic growth. However, the economy is benefiting from a stabilisation of oil prices and foreign exchange rates and lower levels of inflation and, after having contracted by 2.5% in 2015 and 0.2% in 2016, GDP grew by 1.6% in 2017 with further growth of 1.7% forecast in 2018.

In Australia, investment activity has been adversely affected by the downturn in the Mining sector, but the broader economy has been driven by increased public and consumer spending. In 2018, despite expectations that consumption growth will be more subdued, GDP growth is forecast to increase to ca. 3.0% (2017: 2.3%), supported by increases in resource sector capacity and investment in public infrastructure.

## SEALS

### HIGHLIGHTS FROM THE YEAR

- Sector revenue growth of 7%; underlying growth of 10% after adjusting for currency and the net impact from acquisitions and a disposal completed during the past two years
- In North America, Aftermarket underlying revenues increased by 9%, driven by strong markets in the core Hercules business and continued robust growth in the HKX business
- Industrial OEM underlying revenues in North America increased by 13% in a very strong US industrial market, supported by healthy manufacturing PMI data
- Implementation of a new ERP system in the Industrial OEM businesses in the US, following the establishment of a senior management team last year to manage this cluster of businesses
- International Seals businesses increased underlying revenues by 7% with stronger trading across all businesses in the second half of the year

### SECTOR PERFORMANCE

Reported revenues of the Seals Sector businesses increased by 7% to £208.0m (2017: £195.3m). The acquisitions of PSP and Edco completed in 2017, net of a small disposal this year, contributed £3.3m or 2% to Sector revenues, but this was more than offset by currency movements on translation of the results from overseas businesses to UK sterling, which reduced Sector revenues by 5%. After adjusting for the acquisitions and for currency effects, underlying revenues increased by 10%.

Adjusted operating margins for the Sector increased by 100bps to 17.3% (2017: 16.3%) with stronger revenues providing operating leverage. This more than offset a small reduction in gross margins arising from both a lag in the first half of the year in passing on supplier price increases and increased freight costs from expediting inventories. Adjusted operating profits increased by 13% to £36.0m (2017: £31.9m).

During the year, £2.0m (2017: £1.1m) of capital expenditure was invested in the Seals businesses. This primarily comprised £1.1m on implementing a new single ERP system across the US Industrial OEM businesses and a new ERP system in Kentek. A further £0.9m was spent on upgrading warehouse equipment and facilities and on the general IT infrastructure across the Seals businesses. The free cash flow generated in this Sector increased by £1.0m to £25.9m, with stronger operating cash flow being partly absorbed by higher working capital to support the strong trading environment.

#### North American Seals

The North American Seals businesses, which account for 60% of Seals revenues, reported revenues up 6% on the prior year. Underlying revenues increased by 11%, after adjusting for the strengthening of UK sterling against both the US and Canadian dollar, for the disposal of a small non-core business in June and the bolt-on acquisition of PSP completed last year.

The HFPG Aftermarket businesses increased revenues by 9% on a constant currency basis, driven by strong trading conditions in the core Hercules business in both the US and Canada and continued robust growth in the HKX attachment kit business. There was significant pick-up in activity in the Oil & Gas sector and both new Construction and large Infrastructure projects led to increased demand for heavy machinery that required increased servicing and repair. The significant increase in activity has led to extended lead times in the supply chain and robust supplier price increases, which HFPG has sought to mitigate through increased catalogue prices.

In the domestic US market, Hercules revenues increased by 9% with the Repair and Distributor segments growing steadily through the year reflecting higher equipment levels. With seal manufacturers struggling to keep up with demand, Distributors turned to Hercules for their superior service and inventory availability. Hercules continue to add products to their portfolio and broaden the scope of equipment supported to include Aerial-Lifts, Logging, Injection Moulding and Agriculture. Investment was also made to enhance existing sales resources and extend into new territories. New market opportunities include seal kitting services for industrial plants of OEMs. E-commerce continues to deliver strong year-on-year growth and now accounts for 30% of invoices processed and 25% of Hercules US revenues. Enhancements were made to the E-commerce functionality to allow customers to configure custom seals and provide access via mobile applications.

The core Hercules business in the US has also made good progress in developing a major project to invest ca. US\$10m in a second warehouse facility to provide capacity to meet the growing demand for a broader range of products, as well as gain greater access to expanded territories in the US. Potential facilities have been identified and work on this project will commence in 2019 with the aim of becoming fully operational in the 2020 financial year.

In Canada, revenues increased by 7% in local currency terms, supported by a robust Construction sector with increased residential housing starts driving growth in the repair market. Non-residential construction also grew with several new mining projects and demand for additional warehouse facilities. Robust industrial markets had a positive impact on revenues from sales to OEM cylinder manufacturers.

In markets outside of North America, Hercules achieved a double-digit increase in revenues from sales in Colombia and Chile and record sales to the Rest of World, including China.

Revenue (£m)  
(Compound growth over five years)

+14%op.a.

### REVENUE

£208.0m

	2018	2017	
Revenue	£208.0m	£195.3m	+7%
Adjusted operating profit	£36.0m	£31.9m	+13%
Adjusted operating margin	17.3%	16.3%	+100bps
Free cash flow	£25.9m	£24.9m	+4%
ROATCE	25.3%	22.8%	+250bps

The HKX attachment kit business has continued to benefit from tight availability of OEM excavator equipment. In this environment revenues increased by 13%, with strong demand for Tier 3 machines in Canada (ahead of the Tier 4 mandate on 1 January 2019).

In June 2018, Hercules sold its small Bulldog gasket business at net asset value for cash consideration of £4.0m as it was no longer a core part of the Hercules business.

The HFPG Industrial OEM businesses in North America increased revenues by 13% in a very strong US industrial market, supported by healthy Manufacturing PMI data. The business has a number of large key accounts across a range of specialised industrial applications in industries including Water, Medical, Oil & Gas, Fluid Handling and Food Equipment. Good double-digit growth was achieved in all these accounts through deeper and broader penetration to identify additional value-adding opportunities. The businesses continue to provide high levels of customer service and technical support to service existing projects, while looking for opportunities to deploy higher specification, regulatory-compliant compounds, to target new projects with higher levels of added-value.

A constant challenge during the year was managing supplier price increases against a background of generally annual customer supply agreements, particularly with the larger key accounts. The introduction of US tariffs towards the end of the financial year has initially also led to some pressure on gross margins, as existing inventory works through. Tariff charges are now being passed on to customers in the form of a separate line charge and selling prices will be updated as supply agreements are renewed.

The Industrial OEM Seals businesses now comprise a cluster of businesses led by a single senior management team directing the key functions of Sales, Supply Chain, Technical and Finance, while maintaining the distinct identity of each business. This has provided the opportunity to realign sales resources and consolidate the supply chain and finance functions within one back office. A key and necessary part of this exercise was the implementation of a new ERP system to replace the disparate legacy IT systems in the businesses. The new ERP system, which went live shortly after the year end, will increase operational efficiency and improve business intelligence to allow field sales to focus on higher margin market segments and products. These initiatives will be supported by new branding and through strategic advertising and trade shows.

### International Seals

The International Seals businesses, which account for 40% of Seals revenues, reported a 7% increase in UK sterling terms, benefiting from substantially stronger revenues in the second half of the year. After adjusting for currency effects, the impact from the disposal of the Bulldog business on FPE revenues and the acquisition of Edco completed last year, underlying revenues were also up 7%. During the year the International Seals cluster of businesses strengthened management, set up projects to implement new ERP systems in 2019 and shared best practice in developing E-commerce functionality across the businesses.

The FPE Seals and M Seals businesses, with their principal operations in the UK, Scandinavia and the Netherlands, together delivered underlying growth of 6% in revenues on a constant currency basis and after adjustment for the acquisition of Edco and disposal of Bulldog. The FPE Seals business delivered modest underlying revenue growth, despite robust growth in its core UK Aftermarket hydraulic seals and cylinder parts business and a strong improvement in the Oil & Gas market. This was offset by weaker international sales reflecting the absence of a large export order delivered last year. Sales coverage has now been realigned to focus on account management and the existing capacity for the production of machined seals will be utilised to help penetrate the small OEM and Repair businesses outside the hydraulic cylinder market.

M Seals continued to deliver good growth in revenues from its core markets driven by strong customer relationships that have provided a number of major new projects, particularly in Sweden. As with FPE Seals, M Seals has also benefited in the UK from the recovery in the Oil & Gas market with customers expanding activities and providing good growth in revenues. In its first full year with the Group, Edco (now collectively branded M Seals UK) delivered good growth in revenues on a like-for-like basis, with increased sales to key customers.

Kubo, which operates in Switzerland and Austria, increased underlying revenues by 13%, benefiting from strong industrial production driven by increased exports and supported by the depreciation of the Swiss franc. Customers and suppliers reported full order books with production capacity at high levels. Kubo continues to target smaller manufacturing plants focused on Life Sciences, Biotechnology and Microelectronics where Kubo's specialised products and technical knowledge can add value to the customer. During the year, Kubo

### POTENTIAL FOR GROWTH

Continue to gain share in Aftermarket Seals in North America through superior marketing and new products

Leverage E-commerce best practice from North America across International Seals businesses

Build and expand the group of Industrial OEM Seals businesses in North America and leverage procurement activities with the International Seals businesses

Explore opportunities more broadly in Industrial Distribution in North America

Build larger, broader-based International Seals business in the EMEA and Asia-Pacific regions

gained a large new distribution supply contract representing a pan European manufacturer that will provide further opportunity for growth next year. The market in Austria has also been buoyant and Kubo has continued to increase revenues from existing and new customer contracts.

The Kentek business, with principal operations in Finland and Russia, increased revenues by 1% in Euro terms, despite the significant impact on the region from the EU/US sanctions regime. Revenues generated in Russia, which account for ca. 65% of Kentek revenues, improved strongly in the second half of the year, after a weak first half, supported by stronger global Oil & Gas markets. Kentek has also benefited significantly from expanding its own-brand filter range and from widening its geographical coverage towards eastern Russia. In Finland, revenues also increased with sales targeted to support projects in the large Industrial OEM sector.

WCIS has core capabilities in industrial gaskets and mechanical seals used in MRO operations in complex, high specification and arduous conditions. Revenues were negatively impacted this year by cost reduction initiatives in the nickel mining and processing operations of its major customer in New Caledonia. This more than offset strong growth in Australian revenues as new contracts were gained in the Power Generation sector and as Mining activity continued to improve with repairs of customer assets. WCIS continues to broaden its coverage across a wider range of products, market sectors and regional territories.

# CONTROLS

THE CONTROLS SECTOR BUSINESSES SUPPLY SPECIALISED WIRING, CABLE, CONNECTORS, FASTENERS AND CONTROL DEVICES USED IN A RANGE OF TECHNICALLY DEMANDING APPLICATIONS

## GEOGRAPHY

57%	UK
32%	Continental Europe
11%	Rest of World

## CUSTOMERS

31%	Aerospace & Defence
30%	Industrial
13%	Food & Beverage
14%	Motorsport
5%	Energy & Utilities
5%	Medical & Scientific
2%	Rail

## PRODUCTS

45%	Wire & Cable
22%	Fasteners
11%	Connectors
12%	Equipment & Components
9%	Control Devices
1%	Other Controls

## INTERCONNECT

The IS-Group, Filcon, Cablecraft and FS Cables businesses supply high performance electrical interconnect products used in technically demanding applications in a range of industries including Aerospace & Defence, Motorsport, Energy, Medical, Rail and Industrial. A high proportion of the products supplied are used in refurbishment, upgrade and maintenance programmes for equipment in service. Products include electrical wiring, cable, protective sleeving, connectors and harnessing products and customised assemblies. A range of value adding activities enhances the customer offering, including marking of protective sleeves and cables, customised labelling solutions, cut-to-length tubing, kitting, connector assembly and prototype quantities of customised multi-core cables. There is also a range of internally manufactured products, including flexible braided products for screening, earthing and lightning protection, power shunt connectors, multi-core cables, cable markers, sleeving and trunking.

## SPECIALTY FASTENERS

The Clarendon business supplies specialty aerospace-quality fasteners to the Civil Aerospace (focus on aircraft seating and cabin interiors), Motorsport and Industrial & Defence markets. Clarendon supports its key customers with its automated inventory replenishment solution ("Clarendon AIR") utilising bespoke dispensing racks located within the customers' production cells.

## FLUID CONTROLS

The Hawco Group businesses supply a range of fluid control products used broadly in the Food & Beverage sectors, in applications including food retailing and transportation, catering equipment, vending machines, coffee brewing, pure

water and water cooling systems.

Products include fluid controllers, compressors, valves, temperature and pressure measurement devices and specialised vending and liquid dispensing components. The customer offering is enhanced by value adding services including kitting for production line flow and the repair and refurbishment of soft drinks dispensing equipment.

## MARKET DRIVERS

### Industrial economic background

The Controls businesses focus on specialised, technical applications in a range of industries, with ca. 90% of Sector revenues generated in the UK and Continental Europe (principally Germany). The background market drivers are therefore the growth of the industrial economies in the UK and Germany.

A good indicator of the health of the UK industrial economy is the UK Index of Production. Following the 2009 recession, gains in 2010 were reversed in 2011 and 2012 and, except for a period of reduced activity in 2015, since then there has been slow, steady growth. However, the index is still some 7% below pre-recession levels and over the period 2012 to 2017, economic growth has been primarily driven by the Services and Retail sectors.

In Germany, the Production Sector Output index tracks a strong period of recovery through 2010 and 2011, since when it has slowly increased and is now ca. 5% above pre-recession levels.

### Specific industry drivers – Interconnect and Specialty Fasteners

Although influenced by the general industrial economic cycles, there are also more specific drivers within the main market segments served by the Interconnect and Specialty Fasteners businesses.

## Principal operations

### Interconnect

IS-Group	Swindon, UK
IS-Rayfast	Weston-super-Mare, UK
IS-Cabletec	Stuttgart, Germany
IS-Sommer	Indianapolis, IN, US
IS-Connect	Munich, Germany
Filcon	Houghton Regis, Tewkesbury & Plymouth, UK
Cablecraft	St Albans, UK
FS Cables	

### Specialty Fasteners

Clarendon	Leicester, Swindon & Totnes, UK; Huntington Beach, CA, US
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### Fluid Controls

Hawco Group	Godalming, Bolton & Faringdon, UK
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The Civil Aerospace market continues to grow steadily with growth in world passenger traffic averaging over 6% p.a. over the last five years and with continuing strong order books at Boeing and Airbus. The demand for new aircraft is being driven by the need to replace ageing fleets with more fuel-efficient aircraft and the demand from airlines in China and the rest of the Asia-Pacific region. There is increased activity in the cabin interiors market, where the wide range of complex seating and entertainment systems is driving growth.

In the Defence sector, the UK remains committed to maintaining the NATO spend target of 2% of GDP and defence spending is forecast to increase by an average of 1.3% p.a. in real terms through to 2021. In Germany, in response to the emergence of new perceived threats and pressure to meet NATO's spending target, the government has pledged to increase defence spending from ca. 1.2% of GDP in 2018 to ca. 1.5% of GDP in 2024.

In Motorsport, the major drivers of demand in Formula 1 are the number of races (which increased in the 2018 season) and teams (which remained unchanged in the 2018 season) and the level of development work related to technology and rule changes (which, after significant changes in 2017, were not substantial in the 2018 season). The businesses do supply to other motor racing series, however, the spend is relatively low in these series compared to Formula 1.

In the UK, where the current five-year funding control period runs until April 2019, investment in Rail infrastructure continues with electrification projects, station upgrades, line upgrades and the final stages of the Crossrail project. In addition, the design phase of the first stage of the High Speed Two ("HS2") project has commenced, with construction work expected to run through to 2033. More generally, UK infrastructure investment is expected to continue with more than £240bn of investment planned between 2017/18 and 2020/21 and a particular focus on transport, energy and utilities. In Germany, electricity generation and distribution remains a positive sector due to the fragmented nature of the local supply of electricity, where it is the responsibility of towns and cities.

**Specific industry drivers – Fluid Controls**  
The Fluid Controls businesses generate ca. 70% of their revenues from the Food & Beverage sector in the UK. In Food Retailing, the trend away from major out-of-town stores to convenience stores

and home delivery continues. There is also a drive in the Retail industry to reduce energy consumption and to introduce low Global Warming Potential ("GWP") refrigerants to comply with EU F-Gas regulations roadmap through to 2022. In 2018, as a first step to the implementation of tighter regulation, the International Electrotechnical Commission voted to increase charge limits in flammable refrigerants. These trends are driving demand for smaller, more energy efficient components as supplied by Hawco.

The Coffee market sector saw continued growth of ca. 7% in 2017 and is forecast to grow at ca. 5.5% p.a. over the next four years with Abbeychart supplying both the coffee machine manufacturers and the Aftermarket sector, predominately in the UK but also in Europe. The Vending market sector continues to see modest growth, driven by the sale of premium products, particularly in the hot drinks segment.

## CONTROLS

### HIGHLIGHTS FROM THE YEAR

- Sector revenue growth of 9%; underlying growth of 5% after adjusting for currency and acquisitions completed this year
- The Interconnect businesses delivered underlying growth of 7%; the FS Cables acquisition brings a range of own-branded specialist wire and cable products
- Clarendon increased underlying revenues by over 8%, with growth driven by broadening its range of customers in Civil Aerospace; US market targeted through the acquisition of Coast
- Fluid Controls revenues reduced by 4% reflecting the decision to focus on higher margin business and the absence of a large one-off project

### SECTOR PERFORMANCE

Reported revenues of the Controls Sector businesses increased by 9% to £142.4m (2017: £130.7m). The acquisitions of Coast, acquired in October 2017 and FS Cables, acquired in August 2018, added £5.1m or 4% to Sector revenues. After adjusting for negligible currency movements on revenues from translation to UK sterling and for these acquisitions, underlying Sector revenues increased by 5%, with activity in the final quarter particularly robust in what is normally a slower summer period.

Adjusted operating margins were unchanged at 17.6% (2017: 17.6%). Gross margins improved overall reflecting a stronger customer mix in Clarendon, the absence in Fluid Controls of a large low margin project last year, together with a focus away from lower margin air conditioning business. In Interconnect, stronger gross margins in the Cablecraft business offset the impact of strategic pricing used selectively by the IS-Group to penetrate new customers within the broader European region. Investment in sales resources to drive growth for Clarendon in the US and to enhance E-commerce at Cablecraft contributed to an increase in operating costs ahead of revenue. Adjusted operating profits increased by 9% to £25.0m (2017: £23.0m).

Capital expenditure in Controls increased to £1.1m (2017: £0.2m), with £0.7m invested in the IS-Sommer freehold facility to expand the existing warehouse and office capacity. A further £0.4m was invested in small refurbishment projects at both Cablecraft and Clarendon's newly acquired US facility and in product testing equipment in the UK businesses. Free cash flow increased by 6% to £19.8m (2017: £18.6m) reflecting stronger trading and the additional contribution from the acquisitions, partly offset by higher capital expenditure.

### Interconnect

The Interconnect businesses account for 59% of Controls revenues and reported an increase in revenues of 9% in UK sterling terms. After adjusting for the FS Cables acquisition and for currency effects, underlying revenues increased by 7% with good growth in the IS-Group and Cablecraft, more than offsetting the absence of major project activity in Filcon.

The IS-Group's UK businesses reported a 18% increase in revenues reflecting good success achieved in broadening its customer base across the broader European region, through directly targeting cable harness houses, as well as supplying the traditional network of European sub-distributors. In Aerospace and Defence, the UK businesses reported a strong increase in revenues supported by high value repeat orders and new project wins to expand market share. New projects included the design-in of manufactured cables into the KC-46 refuelling tanker, as well as harness components used on the "Crowsnest" Merlin helicopter and the Ajax armoured fighting vehicle. An active Industrial sector also contributed to a strong growth in revenues from a broad range of end-users. In Energy, the recovery in the oil price has led to renewed activity with demand for products going into subsea applications and Tier 4 engines used in the global fracking and mining industries. In Motorsport, revenues were flat on the prior year with a much quieter year for development in Formula 1, WRC and the America's Cup, but were partly compensated by additional activity in Formula E.

The IS-Group's German business, IS-Sommer, delivered 12% growth in revenues with particularly strong performances in the Aerospace, Defence and Industrial markets. A new distribution agreement was concluded during the year with a leading manufacturer of specialist aviation cables, which boosted Aerospace growth. Defence revenues benefited from supplying into new programmes to refit and refurbish Leopard II tanks and Boxer armoured vehicles, as well as the ongoing programme to produce Boxer armoured vehicles for the Lithuanian military. Industrial revenues benefited from the strength of the export led German economy. Medical revenues continued to benefit from design-in efforts initiated in earlier years to help manufacturers manage strict new European regulations for medical devices.

Revenue (£m)  
(Compound growth over five years)

+11%op.a.

### REVENUE

£142.4m

	2018	2017	
Revenue	£142.4m	£130.7m	+9%
Adjusted operating profit	£25.0m	£23.0m	+9%
Adjusted operating margin	17.6%	17.6%	-
Free cash flow	£19.8m	£18.6m	+6%
ROATCE	29.8%	32.2%	-240bps

Motorsport sales remained depressed as a result of the withdrawal of Audi and Volkswagen from the German DTM series. IS-Sommer was also successful in extending its distribution contract with its main supplier of Energy tubing products to a much larger region within Germany, which will provide additional opportunities for growth.

Following over 30% revenue growth last year, Filcon had a tough year with a 26% decrease in revenues due to the absence of major project activity, as well as much lower Motorsport sales following the withdrawal of Audi and Porsche from the Le Mans series and Volkswagen from the World Rally Championship.

Cablecraft reported a 5% increase in revenues as it continued to target new end-user customers including panel builders, switchgear manufacturers, Industrial OEMs and Contractors. During the year the business also focused on substantially refreshing its brand offering and marketing strategy, to be supported by the launch of an enhanced E-commerce website in the first quarter of the new financial year to target a broader range of customers in both the UK and overseas. The facility was also upgraded, creating an expanded and more efficient sales office and relocating the Identification Solutions department to an improved environment that will help drive future growth.

In August 2018, the Group acquired FS Cables, an established and leading supplier of specialist cable products to installers, end-users and wholesalers for a range of industries including Electrical Contracting, Home Automation and Building Management, Rail, Marine and Telecommunications. Based in St Albans, UK, the business primarily supplies own-branded products, which are sourced from a portfolio of long-standing suppliers. These products complement Cablecraft's range of cable accessory products and will provide cross-selling opportunities to both businesses.

After the year end, in October 2018, the IS-Group acquired Gremtek, a long established and leading supplier of own branded protective sleeving and cable identification products to a broad range of industrial markets principally in France, but also in Germany and elsewhere in Europe. Gremtek's principal location is in Paris, France, supported by a facility in Quickborn, Germany. The business will be integrated into the IS-Group to support the strategy of developing a broader Interconnect business across Europe.

#### Specialty Fasteners

The Clarendon Specialty Fasteners business now accounts for 21% of Controls revenues. The acquisition in the US of Coast Fabrication Inc (rebranded Clarendon Specialty Fasteners Inc) in October 2017 contributed to a 25% increase in revenues. After adjusting for this acquisition, underlying revenues increased by 8% with growth driven principally from increased demand from customers in a buoyant Civil Aerospace sector. In this sector Clarendon continued to broaden its customer base of major aircraft seating and cabin interior manufacturers and their sub-contractors across Europe and Asia. Clarendon supports its major customers by supplying its product through its automatic inventory replenishment system ("Clarendon AIR"). During the year, the number of sites operating this system doubled, enabling Clarendon to better service these customers' requirements and providing opportunities for further growth.

In Clarendon's other major market of Motorsport, underlying revenue growth from Formula 1 customers was held back by the absence of any major rule changes in 2018. However, new revenue opportunities arose in projects undertaken for "supercar" development with major automotive OEMs. Good revenue growth was also achieved in the supply of pre-assembled and captive fasteners and bespoke engineered solutions to the Defence and Industrial sectors.

The US business acquired at the beginning of the year has made a good contribution, with particular success in the Space Technology sector. The US business also provides a base to build on the success Clarendon has achieved in the aircraft cabin interiors market in Europe by targeting the US based manufacturers and their subcontractors. The strong Motorsport focus complements Clarendon's existing Motorsport customer base and provides opportunities to increase market share from a more focused sales approach. During the year, investment was made to strengthen sales resources, refurbish the facility and upgrade IT systems to provide a platform for growth.

#### Fluid Controls

The Hawco Group of Fluid Controls businesses accounts for 20% of Controls revenues and supplies temperature, pressure and fluid control products, principally to the Food & Beverage industry. Revenues decreased by 4% against the prior year reflecting the absence of a large one-off project delivered last year and the decision to focus on higher margin products and pull-back from the highly price competitive air conditioning business.

#### POTENTIAL FOR GROWTH

**In Interconnect, create a broader-based European cable harnessing components business and extend product range with own-branded products**

**In Interconnect develop cross-selling opportunities between Cablecraft and FS Cables to drive future growth**

**In Specialty Fasteners, build on strong positions in Civil Aerospace and Motorsport, with a particular focus on the US and Asian markets**

**In Fluid Controls, target the business to grow export markets in the Food & Beverage industry**

Hawco experienced a challenging year with weaker activity in the OEM Refrigeration equipment market as key accounts suffered from a softer UK Food Retail market, caused by the low level of new store openings. Sales to the hospitality trade also slowed as chains embarked on programmes to rationalise branches and cannibalise equipment. In the Contractor market, revenues decreased as Hawco focused on the higher margin products and pulled back from the lower margin air conditioning and cold-room business. However, revenues from the Industrial OEM market increased through a focus on core product lines and on developing broader export markets.

Abbeychart reported strong trading in its core markets, although revenue growth was held back by the absence of a large one-off project delivered last year refreshing a range of vending machines. After adjusting for this project, Abbeychart achieved strong revenue growth by focusing on its value added services, such as refurbishment, kitting and assemblies and through improved marketing. In particular, good growth was achieved in the Water, Vending and Soft Drinks sectors where Abbeychart continues to take market share. Abbeychart also continues to strengthen its relationships with key vending machine operators in Europe through the supply of its range of spare parts for Wurlitzer vending machines.

## FINANCE REVIEW

NIGEL LINGWOOD GROUP FINANCE DIRECTOR

# MAINTAINING FINANCIAL DISCIPLINE

// THE GROUP DELIVERED  
ANOTHER YEAR OF STRONG  
UNDERLYING REVENUE  
GROWTH OF 7% //

### ADJUSTED OPERATING MARGIN

17.5%

### FREE CASH FLOW

£60.5m

### ROATCE

24.5%

### REPORTED AND UNDERLYING RESULTS IN 2018

Reported revenues increased by 7% to £485.1m and adjusted operating profit increased by 9% to £84.9m, with each Sector benefiting from a favourable macroeconomic environment leading to robust customer demand in all geographies.

A recovery this year in UK sterling, particularly in the first half of the year, led to a currency headwind of 3% on the translation of the results of the overseas businesses, when compared with last year's average exchange rates. This currency headwind led to a reduction in revenues and adjusted operating profits of £13.1m and £2.4m, respectively. Acquisitions completed this year and last year, net of a small disposal this year, incrementally contributed £14.8m and £2.1m to revenue and adjusted operating profit, respectively.

The underlying results present the performance of the Group on a like-for-like basis by adjusting for the contribution from businesses acquired during the year (and from the incremental impact from those acquired last year) and for the impact on the translation of the results of the overseas businesses from the strengthening in the UK sterling exchange rate, against most of the currencies of the Group's overseas businesses. With the currency headwind being broadly offset by the incremental contribution from acquisitions (net of a small disposal), underlying revenues and underlying adjusted operating profits also increased by 7% and 9%, respectively.

### ADJUSTED OPERATING MARGIN

The Group's adjusted operating margin improved by 20bps this year to 17.5% (2017: 17.3%) reflecting the benefit of operational leverage, with Group gross margins remaining unchanged from last year.

In Life Sciences, gross margins strengthened slightly, reflecting a more favourable product mix and a small net currency transactional benefit from movements in exchange rates. The Canadian and Australian exchange rates have generally remained more stable this year and the benefit of favourable currency hedge contracts made a positive contribution. In Seals, gross margins slightly weakened as buoyant markets led to supplier price increases and longer product lead times. These price increases were generally not passed through to customers until the second quarter of the financial year. Freight costs also increased to mitigate longer lead times and maintain service levels to customers. In Controls, gross margins improved reflecting the benefit from a favourable product mix, proactive and targeted price increases and a decision to pull back from lower margin sales opportunities.

#### ADJUSTED AND STATUTORY PROFIT BEFORE TAX

Adjusted profit before tax increased by 9% to £84.8m (2017: £77.5m). The interest expense this year was £0.1m (2017: £0.7m) and comprised the interest expense on the Group's net pension deficit, which had reduced from £0.3m last year, reflecting the smaller deficit in the fund at the beginning of this year.

There were no borrowing costs this year (2017: £0.1m) as the Group held cash funds for the majority of the year and interest earned on these cash funds of £0.1m offset bank facility commitment fees of £0.1m (2017: £0.3m). Last year's facility fees included a £0.2m arrangement fee on renewal of the bank facility.

Statutory profit before tax was £72.7m (2017: £66.8m) and is after charging acquisition related charges of £9.6m (2017: £9.7m) (which largely comprises the amortisation of acquisition related intangible assets) and fair value remeasurements of £0.4m (2017: £1.0m). In addition, one-off CEO transition costs of £2.1m were incurred relating to the change of the CEO in the current year.

The CEO transition costs comprise those charges directly attributable to the change, after 22 years, in the leadership of the Group this year. In particular, it includes the costs of recruitment, the costs of employment of the new CEO and the costs of the financial settlement relating to his departure from the Company on 28 August 2018, including advisors costs. These costs are set out

in note 28 to the consolidated financial statements. The full year employment costs of Bruce Thompson, the retiring CEO, have been charged against adjusted operating profit and are not included in CEO transition costs.

The charge attributable to fair value remeasurements relate to the put options held over minority interests as described further below.

#### TAX CHARGE, EARNINGS PER SHARE AND DIVIDENDS

The Group's effective tax charge on adjusted profit reduced by 260bps in 2018 to 23.9%, compared with 26.5% last year. This lower rate reflected the impact from the reduction in the US Federal corporate income tax rate to 21% from 35%, effective 1 January 2018. The adjusted profit before tax earned in the US accounts for ca. 26% of Group adjusted profit before tax.

Adjusted earnings per share ("EPS") increased by 13% to 56.4p, compared with 49.8p last year and statutory EPS increased by 13% to 47.5p (2017: 42.0p).

The Board continues to pursue a progressive dividend policy that aims to increase the dividend each year broadly in line with the growth in adjusted EPS. In determining the dividend in any one year, the Board also considers a number of factors which include the strength of the free cash flow generated by the Group, the future cash commitments and investment needed to sustain the Group's long term growth strategy and the target level of dividend cover. The Board continues to target towards two times dividend cover (defined as the ratio of adjusted EPS to total dividends paid and proposed for the year), which provides a prudent buffer. The ability of the Board to maintain future dividend policy will be influenced by the principal risks identified on pages 30 to 33 that could adversely impact the performance of the Group.

For 2018, the Board has recommended a final dividend of 17.8p per share (2017: 16.0p) making the proposed full year dividend 25.5p (2017: 23.0p). This represents an 11% increase in the proposed full year dividend with dividend cover remaining unchanged at 2.2 times.

## FINANCE REVIEW CONTINUED

### FREE CASH FLOW

Free cash flow represents cash available to invest in acquisitions or return to shareholders. The Group again generated strong free cash flow this year of £60.5m (2017: £55.7m), which benefited from £4.0m received on the sale of the small non-core US business. The free cash flow conversion was 95% (2017: 99%) of adjusted earnings.

The Group's operating cash flow increased by £5.0m to £84.3m (2017: £79.3m) this year, broadly reflecting the increase in operating profit. As anticipated in the Half Year Report, the outflow of cash into working capital reduced substantially in the second half of the year to £5.1m (2017: £4.0m) from £11.2m at 31 March 2018. Inventories increased by £8.3m (2017: £5.1m) to meet the stronger trading environment, particularly in the Seals businesses. This was partly offset by an inflow of £3.2m (2017: £1.1m) from an increase in net payables at the year end. The Group's KPI metric of working capital to revenue at 30 September 2018 remained broadly unchanged from last year at 15.1% (2017: 15.0%), again reflecting the robust revenues over the previous rolling 12 months.

Group tax payments decreased by £0.3m to £19.0m (2017: £19.3m). On an underlying basis cash tax payments represented ca. 23% (2017: 24%) of adjusted profit before tax reflecting the benefit from the lower US Federal corporate income tax rate. Underlying tax payments are before currency effects from translation and exclude payments for pre-acquisition tax liabilities in acquired businesses.

The Group's tax strategy is to comply with tax laws in all of the countries in which it operates and to balance its responsibilities for managing tax, with its responsibility to pay tax where it does business. The Group's tax strategy and policies have been approved by the Board this year and tax risks are regularly reviewed by the Audit Committee.

The Group's capital expenditure doubled this year to £6.6m (2017: £3.3m) reflecting in part the impact from new field equipment introduced in the Healthcare businesses and in part investment required in facility and IT infrastructure across the Group to support the increased trading activity seen over the past two years.

The Life Sciences businesses invested £3.5m in new capital this year (2017: £2.0m) of which £2.3m (2017: £1.6m) was invested in field equipment in the Healthcare businesses to support placements of new surgical equipment in hospitals and diagnostic machines in laboratories. A further £0.6m was invested in expanding and refurbishing facilities and offices in both the Healthcare and Environmental businesses and the remaining £0.6m on both warehouse equipment and on upgrading the IT infrastructure.

The Seals businesses invested £2.0m (2017: £1.1m), with £1.5m in the North American Seals businesses and £0.5m in the International Seals businesses. The new ERP systems being implemented in both the US Industrial OEM Seals business and in Kentek accounted for £1.1m and £0.8m was spent on refurbishing facilities and on warehouse equipment. The remaining £0.1m was spent on upgrading the IT infrastructure across the Seals Sector. In the Controls businesses £1.1m (2017: £0.2m) was invested primarily in expanding and refurbishing existing facilities. In particular the German business, IS-Sommer, invested £0.7m on expanding its existing warehouse and offices in Stuttgart, which is expected to be completed for a total cost of ca. £1.6m in March next year. The remaining £0.4m was spent on refurbishing the facilities in Cablecraft and Coast.

The Company paid the PAYE income tax liability of £1.0m (2017: £0.7m) on the exercise of LTIP share awards in November 2017, in exchange for reduced share awards to participants. In addition, £1.2m was paid to the Employee Benefit Trust to fund the

acquisition of 100,000 ordinary shares in the Company to meet incentive awards.

The Group spent £20.4m (2017: £20.1m) of free cash flow on acquisitions, including £2.0m on acquiring outstanding minority shareholdings, as described below and £27.0m (2017: £23.7m) on paying dividends to both Company and minority shareholders.

### ACQUISITIONS COMPLETED DURING THE YEAR

The Group invested £18.1m on acquiring new businesses this year and paid a further £0.3m of deferred consideration on businesses acquired in prior years. The continuing favourable economic markets in the US and Continental Europe this year contributed again to a much tougher environment to persuade potential vendors to dispose of their companies. However there were tentative signs towards the end of the year that, having enjoyed several years of stronger trading and with uncertainty about the future direction of global economies, some of these vendors were returning to the M&A market.

In August 2018 the Group completed the acquisition of FS Cables, based in St Albans, UK, for £16.9m on a debt/cash free basis. FS Cables is a leading supplier of specialist cable products to installers, end-users and wholesalers for a range of industries. The business complements the Group's existing Cablecraft business acquired in 2016, which supplies cable accessory products used to identify, secure and protect electrical cables. A further £1.2m was spent in October 2017 to acquire Coast, a small specialty fastener distributor based in California, US.

These acquisitions added £9.1m to the Group's acquired intangible assets, which represents the valuation of customer and supplier relationships that will be amortised over periods ranging from five to ten years. At 30 September 2018, the carrying value of the Group's acquired intangible assets was £53.6m and there was a £9.3m charge this year to amortise these assets.

Goodwill at 30 September 2018 was £128.5m and included £5.7m relating to those businesses acquired during the year (including fair value adjustments to the assets acquired). Goodwill is not amortised, but is assessed each year at a Sector level to determine whether there has been any impairment in the carrying value of goodwill acquired. The exercise to assess whether goodwill has been impaired is described in note 10 to the consolidated financial statements. It was confirmed that there was significant headroom on the valuation of this goodwill, compared with the carrying value of goodwill at the year end.

Shortly after the year end, the IS-Group acquired Gremtek, a supplier of own-branded protective sleeving products based in France for £7.4m. This business will be integrated into the IS-Group to support their expansion into European markets.

#### LIABILITIES TO MINORITY SHAREHOLDERS

The Group's liability to purchase outstanding minority shareholdings at 30 September 2018 reduced to £4.5m (2017: £6.1m) following the purchase of the outstanding 10% minority shareholding in TPD for £2.0m.

The minority shareholdings outstanding at 30 September 2018 relate to a 10% interest held in both M Seals and Kentek. The options are exercisable in the next financial year.

The liabilities for these put options are valued based on the Directors' latest estimate of the earnings before interest and tax ("EBIT") of these businesses when these options crystallise. A charge of £0.4m (2017: £1.0m) has been included in finance expense to reflect in part a slightly higher expected cost of purchasing these minority interests and in part the unwinding of the discount on the liability.

The Group also has a small liability at 30 September 2018 for deferred consideration of up to £1.1m (2017: £0.5m), which represents the Directors' best estimate of the amount likely to be paid to the vendors of businesses purchased during the year, based on the expected performance of these businesses during the measurement period. During the year, £0.3m was paid as deferred consideration relating to the acquisition of Ascome and Edco in previous years and £0.2m, which was no longer required, was released to the Consolidated Income Statement as part of acquisition related charges.

#### RETURN ON ADJUSTED TRADING CAPITAL EMPLOYED AND CAPITAL MANAGEMENT

A key metric used to measure the overall profitability of the Group and its success in creating value for shareholders is the return on adjusted trading capital employed ("ROATCE"). At a Group level, this is a pre-tax measure that is applied against the fixed and working capital of the Group, together with all gross intangible assets and goodwill, including goodwill previously written off against retained earnings. At 30 September 2018, the Group ROATCE remained comfortably ahead of our 20% benchmark and improved to 24.5% (2017: 24.0%), which reflects the strong increase in adjusted operating profit this year. Adjusted trading capital employed is defined in notes 2 and 3 to the consolidated financial statements.

The Group continues to maintain a strong balance sheet with cash funds of £36.0m at 30 September 2018, compared with

£22.3m last year. Surplus cash funds are generally repatriated to the UK, unless they are required locally to meet certain commitments, including acquisitions.

The Group also maintains a three year revolving multi-currency credit facility that expires on 1 June 2020, but has an option to extend the facility up to 1 June 2022. The facility comprises a £30m committed facility with an accordion option that allows the Group to increase the commitment up to a maximum of £60m of borrowings. These facilities have a ratchet margin ranging from 70bps to 115bps over LIBOR, depending on the ratio of EBITDA to net debt. These bank facilities are primarily used to meet any shortfall in cash to fund acquisitions.

#### EMPLOYEE PENSION OBLIGATIONS

Pension benefits to existing employees, both in the UK and overseas, are provided through defined contribution schemes at an aggregate cost in 2018 of £3.1m (2017: £2.8m).

The Group maintains a small legacy closed defined benefit pension scheme in the UK. A formal triennial funding valuation of this scheme was carried out as at 30 September 2016 and reported a funding deficit of £9.2m with a 75% funding level, which reflected the impact of bond yields falling to a record low of 1.5% at the valuation date. Since the valuation date, bond yields have increased to 2.9% and investment returns have been strong, which has led to a lower funding deficit. This deficit is being funded by cash contributions of £0.5m (2017: £0.4m) paid by the Company to the scheme. This contribution rate increases annually on 1 October by 2% with the objective of eliminating the deficit within ten years.

During the year, the scheme trustees, with the support of the Company, completed a buy-in of the pensioner liabilities existing at 1 September 2018. The buy-in was completed on 28 September 2018 with Just Retirement Limited for a premium of £13.0m, which was funded by the scheme, utilising substantial investment gains realised on the scheme's growth assets.

A recent decision by the High Court has confirmed that pension schemes will be required to equalise GMPs accrued between 1990 and 1997, between men and women. The UK scheme has not yet equalised GMPs, although as only ca. 25% of the members were contracted out of SERPS prior to 1997, the impact is unlikely to be material to the schemes existing liabilities.

In Switzerland, local law requires Kubo to provide a contribution based pension for all employees, which are funded by employer and employee contributions. This pension plan is managed for Kubo through a separate

multi-employer plan of non-associated Swiss companies, which pools the funding risk between participating companies. In Switzerland, Kubo's annual cash contribution to the pension scheme was £0.2m (2017: £0.2m).

Both the UK defined benefit scheme and the Kubo contribution scheme are accounted for in accordance with IAS19 (Revised). At 30 September 2018 the aggregate accounting pension deficit in these two schemes increased slightly by £0.6m to £10.5m with a reduction of the deficit in the Swiss scheme being more than offset by an increase in the UK scheme deficit. The larger deficit in the UK scheme is because the buy-in premium was larger than the valuation of the corresponding liabilities; the Swiss scheme benefited from a higher discount rate, which led to a reduction in the scheme deficit. The gross aggregate pension liability in respect of these two schemes at 30 September 2018 decreased by £0.4m to £49.1m, which is funded by £38.6m of assets.

#### POTENTIAL IMPACT OF BREXIT

At an operational level, the impact on the Group's businesses from the current uncertainty over the process and timing of the UK's exit from the European Union is not expected to be significant in terms of the Group's overall profitability. UK based revenues account for only 26% of the Group's overall revenues and the UK businesses, as well as those based in Continental Europe, are substantially "in country" industrial suppliers of goods with limited cross border sales activity.

The Group's financial results may be impacted by macroeconomic instability arising from a delayed or disruptive exit from the European Union, such as a depressed UK economy or a substantial depreciation in UK sterling. In such a scenario, there may be a reduction in the Group's UK revenues and operating profits, although Group net assets would benefit from translating the results of the Group's overseas businesses into UK sterling. It is also likely that a depreciation in UK sterling would lead to stronger inflation in supplier costs for the Group's UK based businesses, which would need to be managed robustly to maintain gross margins.

The Board will continue to monitor closely developments in the Brexit plans on its UK businesses. A prolonged disruption at the UK's borders has the potential to impact the supply chain of the Group's UK businesses; however the businesses maintain a strong depth of inventories and have begun to build inventory levels of their faster moving product lines which would mitigate the impact on their activities from a significant disruption in cross border trade between the UK and Continental Europe.

## INTERNAL CONTROL AND RISK MANAGEMENT

The Board is committed to protecting and enhancing Diploma's reputation and assets, while safeguarding the interests of shareholders. It has overall responsibility for the Group's system of risk management and internal control.

Diploma's businesses are affected by a number of risks and uncertainties. These may be impacted by internal and external factors, some of which we cannot control. Many of the risks are similar to those found by comparable companies in terms of scale and operations.

### OUR APPROACH

Risk management and maintenance of appropriate systems of control to manage risk is the responsibility of the Board and is integral to the ability of the Group to deliver on its strategic priorities. The Board has developed a framework of risk management that is used to establish the culture of effective risk management throughout the businesses by identifying and monitoring the material risks, setting risk appetite and determining the overall risk tolerance of the Group. This framework of risk management has been further enhanced this year and additional processes have been developed, which will assist the Board to monitor and assess the principal risks throughout the year.

The Group's risk management systems are monitored by the Audit Committee, under delegation from the Board. The Audit Committee is responsible for overseeing the effectiveness of the internal control environment of the Group. An Internal Audit function has been established for many years to provide independent assurance that the Group's risk management, governance and internal control processes are operating effectively.

### IDENTIFYING AND MONITORING MATERIAL RISKS

Material risks are identified through a detailed analysis of individual processes and procedures (bottom up approach) and a consideration of the strategy and operating environment of the Group (top down approach).

The detailed risk evaluation process begins in the operating businesses with an annual exercise undertaken by management to identify and document the significant strategic, operational, financial and accounting risks facing the businesses. This process is both robust and challenging; it ensures that risks are identified and monitored and that management controls are embedded in the business' operations.

The Group uses a quantitative method to determine a risk score for each risk which is based on both the likelihood of each identified risk occurring and the consequence of an adverse outcome and its impact on the business. Each business will then identify processes established to control each risk and minimise its potential impact.

The risk assessments from each of the operating businesses are then considered by the Board who evaluate the principal risks of the Group with reference to the Group's strategy and operating environment.

### OUR PRINCIPAL RISKS AND UNCERTAINTIES

Set out in this section of the Strategic Report are the principal risks and uncertainties affecting the Group that have been determined by the Board, based on a robust risk evaluation process described above, to potentially have the greatest impact on the Group's future viability. These risks are similar to those reported last year, although with some movement on the relative ranking of these risks. There were no new principal risks identified from the review process carried out by the Board this year.

The risks are each classified as either strategic, operational, financial or accounting. The Group's decentralised operations with different Sectors and geographical spread reduces the impact of these principal risks.

The Board has also considered the risks associated with the UK's vote to leave the European Union and this is explained further on page 29 in the Finance Review.

### VIABILITY STATEMENT - DIPLOMA PLC

The Directors confirm that they have a reasonable expectation that the Group will continue to operate and meet its liabilities, as they fall due, for the next three years to September 2021. The Directors' assessment has been made with reference to the resilience of the Group and its strong financial position, the Group's current strategy, the Board's risk appetite and the Group's principal risks and how these are managed, as described in the Strategic Report. In October 2018, the Board approved a report on an update of the Group's strategy for the three years ending 30 September 2021, as described on page 40.



The Group has a broad spread of customers and suppliers across different geographic areas and independent market sectors, often secured with longer term agreements. The Group is supported by a robust balance sheet and strong operational cash flows.

The assessment period of three years has been chosen as it is consistent with the Board's triennial review of the Group's strategy at which the prospects of each business are discussed; assumptions are made regarding entering into new markets




and geographies, about future growth rates of the existing businesses and about the acceptable performance of existing businesses. A robust financial model of the Group is built on a business-by-business basis and the metrics for the Group's KPIs are reviewed for the assessment period. These metrics are also subject to sensitivity analysis that includes flexing a number of the main assumptions, namely, future revenue growth, gross margins, operating costs and working capital management. The results of flexing these assumptions, both individually and in aggregate to reflect a reasonable worse case scenario, are used to determine whether additional bank facilities will be required during this period.

The Directors confirm that this robust assessment also considers the principal risks facing the Group, as described on pages 31 to 33 and the potential impacts these risks would have on the Group's business model, future performance, solvency or liquidity over the assessment period. The Board considers that the diverse nature of the Sectors and geographies in which the Group operates acts significantly to mitigate the impact any of these risks might have on the Group.



RISK	RISK DESCRIPTION AND ASSESSMENT	MITIGATION
<b>STRATEGIC RISK DOWNTURN/ INSTABILITY IN MAJOR MARKETS</b>  <b>CHANGE</b> 	<p>Adverse changes in the major markets in which the businesses operate can have a significant impact on performance. The effects of these changes can be seen in terms of slowing revenue growth, due to reduced or delayed demand for products and services, or margin pressures due to increased competition.</p> <p>A number of characteristics of the Group's businesses moderate the impact of economic and business cycles on the Group as a whole:</p> <ul style="list-style-type: none"> <li>• The Group's businesses operate in three differing Sectors with different cyclical characteristics and across a number of geographic markets.</li> <li>• The global economic outlook was more uncertain towards the end of the financial year.</li> <li>• The businesses offer specialised products and services, which are often specific to their application; this offers a degree of protection against customers quickly switching business to achieve a better price.</li> <li>• A high proportion of the Group's revenues comprise consumable products that are purchased as part of the customer's operating expenditure, rather than through capital budgets.</li> <li>• In many cases the products are used in repair, maintenance and refurbishment applications, rather than original equipment manufacturer.</li> </ul>	<p>The businesses identify key market drivers and monitor the trends and forecasts, as well as maintaining close relationships with key customers who may give an early warning of slowing demand.</p> <p>Changes to cost levels and inventories can then be made in a measured way to mitigate the effects.</p> <p>Significant global events are closely monitored to determine any potential impact on key markets.</p>
<b>STRATEGIC RISK SUPPLIER CONCENTRATION/ LOSS OF KEY SUPPLIERS</b>  <b>CHANGE</b> 	<p>For manufacturer-branded products, there are risks to the business if a major supplier decides to cancel a distribution agreement or if the supplier is acquired by a company that has its own distribution channels in the relevant market. There is also the risk of a supplier taking away exclusivity and either setting up direct operations or appointing another distributor.</p> <p>Currently no single supplier represents more than 10% of Group revenue and only five suppliers represent more than 2% each of Group revenue.</p> <p>Relationships with suppliers have normally been built up over many years and a strong degree of interdependence has been established. The average length of the principal supplier relationships in each of the Sectors is over ten years.</p> <p>The strength of the relationship with each supplier and the volume of activity generally ensures continuity of supply, when there is shortage of product.</p> <p>The success of the businesses depends significantly on representing suppliers whose products are recognised in the marketplace as the leading competitive brand. If suppliers fail to support these products with new development and technologies, then our businesses will suffer from reduced demand for their products and services.</p>	<p>Long term, multi-year exclusive contracts signed with suppliers with change of control clauses, where possible, included in contracts for protection or compensation in the event of acquisition.</p> <p>Collaborative projects and relationships maintained with individuals at many levels of the supplier organisation, together with regular review meetings and adherence to contractual terms.</p> <p>Regular review of inventory levels.</p> <p>Bundling and kitting of products and provision of added value services.</p> <p>Periodic research of alternative suppliers as part of contingency planning.</p> <p>The businesses work very closely with each of their suppliers and regularly attend industry exhibitions to keep abreast of the latest technology and market requirements/trends. The businesses also meet with key customers on a regular basis to gain insight into their product requirements and market developments.</p>

## INTERNAL CONTROL AND RISK MANAGEMENT CONTINUED

RISK	RISK DESCRIPTION AND ASSESSMENT	MITIGATION
<b>STRATEGIC RISK</b> <b>CUSTOMER CONCENTRATION/</b> <b>LOSS OF KEY CUSTOMER(S)</b>  <b>CHANGE</b> 	<p>The loss of one or more major customers can be a material risk.</p> <p>The nature of the Group's businesses is such that there is not a high level of dependence on any individual customer and no single customer represents more than 4% of Sector revenue or more than 2% of Group revenue.</p>	<p>Specific large customers are important to individual operating businesses and a high level of effort is invested in ensuring that these customers are retained and encouraged not to switch to another supplier.</p> <p>In addition to providing high levels of customer service and value added activities, close integration is established where possible with customers' systems and processes.</p>
<b>OPERATIONAL RISK</b> <b>CYBERSECURITY/</b> <b>INFORMATION TECHNOLOGY/</b> <b>BUSINESS INTERRUPTION</b>  <b>CHANGE</b> 	<p>Group and operating business management depend critically on timely and reliable information from their IT systems to run their businesses. The Group seeks to ensure continuous availability, security and operation of those information systems.</p> <p>Cyber threats to the businesses information systems have this year reduced, following action taken to strengthen the IT infrastructure environment across the Group's businesses.</p> <p>Any disruption or denial of service may delay or impact decision making through lack of availability of reliable data. Poor information handling or interruption of business may also lead to reduced service to customers. Unintended actions of employees caused by a cyber-attack may also lead to disruption, including fraud.</p> <p>In North American Seals, HFPG's Aftermarket business is operated from a single warehouse based in Tampa, Florida which continues to be exposed to hurricanes during the season from August to November.</p>	<p>There is good support and back-up built into local IT systems and the spread of businesses with their own stand alone IT systems also offers good protection from individual events. The majority of businesses back-up online data at least once a day to an offsite data storage centre.</p> <p>A member of the Executive Management Committee is responsible for ensuring each business in the Group has a robust cybersecurity programme and reports twice a year to the main Board on the status of cybersecurity across the Group. In addition, education/awareness of cyber threats continues to ensure Group employees protect themselves and Group assets. At 30 September 2018, the majority of businesses had achieved the UK Government endorsed Cyber Essentials accreditation; it is expected that all businesses will be fully accredited within the next six months.</p> <p>Business continuity plans exist for each business with ongoing testing.</p>
<b>OPERATIONAL RISK</b> <b>LOSS OF KEY PERSONNEL</b>  <b>CHANGE</b> 	<p>The success of the Group is built upon strong, self-standing management teams in the operating businesses, committed to the success of their respective businesses. As a result, the loss of key personnel can have an impact on performance, for a limited time period.</p> <p>The average length of service of the ca. 100 senior managers in the Group is 11 years and for all personnel in the Group is consistently ca. 7 years.</p> <p>The uncertainty this year relating to the appointment and subsequent departure of the Chief Executive Officer has led to some instability in management and employees within the Group.</p>	<p>Contractual terms such as notice periods and non-compete clauses can mitigate the risk in the short term. However, more successful initiatives focus on ensuring a challenging work environment with appropriate reward systems. The Group places very high importance on planning the development, motivation and reward for key managers in the operating businesses including:</p> <ul style="list-style-type: none"> <li>• Ensuring a challenging working environment where managers feel they have control over, and responsibility for, their businesses.</li> <li>• Establishing management development programmes to ensure a broad base of talented managers.</li> <li>• Offering a balanced and competitive compensation package with a combination of salary, annual bonus and long term cash or share incentive plans targeted at the individual business level.</li> <li>• Giving the freedom, encouragement, financial resources and strategic support for managers to pursue ambitious growth plans.</li> </ul>

RISK	RISK DESCRIPTION AND ASSESSMENT	MITIGATION
<b>OPERATIONAL RISK</b> <b>PRODUCT LIABILITY</b>  <b>CHANGE</b> 	<p>There is a risk that products supplied by a Group business may fail in service, which could lead to a claim under product liability. The businesses, in their terms and conditions of sale with customers, will typically mirror the terms and conditions of purchase from the suppliers. In this way the liability can be limited and subrogated to the supplier.</p> <p>If a legal claim is made it will typically draw in our business as a party to the claim and the business may be exposed to legal costs and potential damages if the claim succeeds and the supplier fails to meet its liabilities for whatever reason. Product liability insurance can be limited in terms of its scope of insurable events, such as product recall.</p> <p>In situations where a Group business is selling own-branded products and cannot subrogate the liability to a supplier, the business will be liable for failure of the product. A Group business may also be liable for the associated costs of a subsequent customer recall arising directly from failure of an own-branded product.</p>	<p>Technically qualified personnel and control systems are in place to ensure products meet quality requirements. The Group's businesses are required to undertake Product Risk assessments and comprehensive Supplier Quality Assurance assessments. The Group has also established Group-wide product liability insurance which provides worldwide umbrella insurance cover of £30m across all Sectors.</p> <p>The Group's businesses have undergone product liability training and are continually reviewed to demonstrate compliance with Group policies and procedures relating to product liability.</p>
<b>FINANCIAL RISK</b> <b>FOREIGN CURRENCY</b>  <b>CHANGE</b> 	<p>Foreign currency risk is the risk that currency rates will affect the Group's results. The Group is exposed to two types of financial risk caused by currency volatility: translational exposure, being the effect that currency movements have on the Group's financial statements on translating the results of overseas subsidiaries into UK sterling; and transactional exposure, being the effect that currency movements have on the results of operating businesses because their revenues or product costs are denominated in a currency other than their local currency.</p> <p>The Group operates internationally and is exposed to translational foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar, the Canadian dollar, the Australian dollar and the Euro. The results and net assets of the Group's operations outside the UK are also exposed to foreign currency translation risk.</p> <p>A strengthening of UK sterling by 10% against all the currencies in which the Group does business, would reduce adjusted operating profit before tax by approximately £6.5m (8%), due to currency translation. Similarly, a strengthening of UK sterling by 10% against all the non-UK sterling capital employed would reduce shareholders' funds by £20.4m.</p> <p>The Group's UK businesses are exposed to transactional foreign exchange risk on those purchases that are denominated in a currency other than their local currency, principally US dollars and Euros. The Group's Canadian and Australian businesses are also exposed to a similar risk as the majority of their purchases are denominated in US dollars and Euros. The Group's US businesses do not have any material foreign currency transactional risk.</p>	<p>The Group operates across a number of diverse geographies but does not hedge translational exposure of operating profit and net assets.</p> <p>The Group's businesses may hedge up to 80% of forecast (being a maximum of 18 months) foreign currency transactional exposures using forward foreign exchange contracts.</p> <p>The Group finance department monitors rolling monthly forecasts of currency exposures.</p> <p>Details of average exchange rates used in the translation of overseas earnings and of year end exchange rates used in the translation of overseas balance sheets, for the principal currencies used by the Group, are shown in note 29 to the consolidated financial statements.</p>
<b>ACCOUNTING RISK</b> <b>INVENTORY OBSOLESCENCE</b>  <b>CHANGE</b> 	<p>Working capital management is critical to success in specialised industrial distribution businesses as this has a major impact on cash flow. The principal risk to working capital is in inventory obsolescence and write-off.</p> <p>The charge against operating profit in respect of old or surplus inventory in the year was £1.5m but inventories are generally not subject to technological obsolescence.</p>	<p>Inventory write-offs are controlled and minimised by active management of inventory levels based on sales forecasts and regular cycle counts.</p> <p>Where necessary, a provision is made to cover both excess inventory and potential obsolescence.</p>

# CORPORATE RESPONSIBILITY

## EMPLOYEES

Building and developing the skills, competencies, motivation and teamwork of employees is recognised by the Board as being essential to achieving the Group's business objectives. The loss of key personnel is also identified by the Board as a principal risk as set out on page 32. The stability and commitment of the employees is demonstrated by the average length of service, which is consistently high at ca. seven years. In addition, the number of working days lost to sickness is ca. 1% a year. These measures remain consistent across each of the Group's Sectors.

### Key employee statistics

	2018	2017	2016
Average number of employees in year	1,765	1,658	1,602
Females as percentage of total	35%	35%	36%
Length of service (years)	6.8	6.7	6.8
Average staff turnover	19.7%	20.6%	24.9%
Sick days lost per person	3.6	3.3	3.1

The Group encourages healthy lifestyles and the level of sick days lost per person is heavily influenced by a small number of employees who are on long term sick leave.

Set out below is an analysis of the number of employees by gender at the year end:

	2018			2017		
	Male	Female	Total	Male	Female	Total
Directors	4	1	5	5	1	6
Senior managers	78	18	96	73	19	92
Employees	1,092	614	1,706	1,048	586	1,634
Total	1,174	633	1,807	1,126	606	1,732

The Board recognises the importance of gender diversity in the Group and 35% of the Group's employees are female. Some of the Group's operating companies have structured apprenticeship schemes and of the ten UK based apprenticeships, three of these were for females.

The Group values the commitment of its employees and recognises the importance of communication to foster good working relationships. The Group keeps employees informed on matters relating to their employment, on business developments and on the financial and economic factors affecting the Group. This is achieved through management briefings, internal announcements, the Group's website and by the distribution of Preliminary and Interim Announcements and press releases.

Copies of the Annual Review and Annual Report & Accounts are also made available in the operating businesses. This communication programme enables employees to gain a better understanding of the Group's business objectives and their roles in achieving them. Both employment policy and practice in the Group are based on non-discrimination and equal opportunities. Ability and aptitude are the determining factors in the selection, training, career development and promotion of all employees.

The Group remains supportive of the employment and advancement of disabled persons. Applications for employment by disabled persons are always fully considered, bearing in mind the respective aptitudes and abilities of the applicants concerned. If an employee is, or becomes disabled during their period of employment, the Group will, if necessary and to the extent possible, adapt the work environment to enable the employee to continue in their current position or retrain the employee for duties suited to their abilities following disablement. At 30 September 2018, the Group employed ten disabled employees (2017: seven).

Employment policies throughout the Group have been established to comply with relevant local legislation and codes of practice relating to employment, Health & Safety and equal

opportunities. The Group provides good quality working environments and facilities for employees and training and development appropriate to each of their roles.

The Group provides sponsorship for high potential employees for higher education courses where appropriate. Vocational training is also provided and some staff are enrolled on National Vocational Qualification ("NVQ") or similar level courses. Employees are actively encouraged to undertake Continuing Professional Development ("CPD") to maintain any relevant professional accreditations.

In accordance with the Market Abuse Regulation of the Financial Conduct Authority, employees are required to seek approval of the Group Company Secretary before dealing in its shares.

## HEALTH & SAFETY

The Group is fully committed to ensuring clean, safe and healthy working conditions. The Group actively promotes a strong safety culture and ensures a collective responsibility for ensuring Health & Safety standards are continually improved.

The Chief Executive Officer assisted by a member of the Executive Management Committee has overall responsibility for Health & Safety policies and procedures across the Group. However, in line with the Group's decentralised management approach, accountability for Health & Safety is with local management to ensure compliance with local regulatory requirements, culture and specific business needs. The Group requires that each operating business conducts Health & Safety reviews against its specific operational risk profile and local regulatory requirements.

Health & Safety forms part of the induction process for new employees and where relevant, more specialist training is provided for specific functions. The Group has good coverage of employees who have formal Health & Safety training and/or qualifications and this has continued to increase during 2018.

Following the implementation of near miss reporting in 2016, the Group has now used its second full year of the system to assist in ensuring that Health & Safety hazards are proactively identified, and appropriate mitigation put in place to ensure that they do not result in Health & Safety incidents.

	2018	2017
Near misses	73	70
Minor injuries	71	56
Reportable lost time incidents <sup>1</sup>	1	5
Minor injuries per 1,000 employees	40.2	33.8
Reportable lost time incidents <sup>1</sup> per 1,000 employees	0.6	3.0

<sup>1</sup> Three or more days' absence from workplace.

The absolute level of minor injuries has increased this year primarily due to a low level reported in the prior year. The near miss reporting system has placed emphasis on the need to identify and implement corrective actions prior to incidents occurring and this methodology indirectly assists with reducing health and safety risk. The vast majority of the minor injuries resulted in no lost time and were considered low level. The number of reportable lost time incidents has also reduced significantly.

All incidents are fully investigated and corrective actions and preventative measures are put in place to ensure that the incident does not reoccur, and future risks are mitigated.

## HUMAN RIGHTS

The Group's activities are substantially carried out in developed countries that have strong legislation governing human rights. The Group complies fully with appropriate legislation in the countries in which it operates to ensure the rights of every

employee are respected and to treat all stakeholders with dignity and respect. The Group promotes employment practices to ensure fair regard to diversity and equal opportunities. Staff are provided with a safe, secure and healthy environment in which to work. Employees have access to an independent hotline to report any issues relating to Human Rights violations.

#### MODERN SLAVERY

The Group adopts a zero tolerance approach to slavery in all its forms, including human trafficking, forced labour and child labour. Annually, each business assesses the risk of slavery taking place either within the business itself or among its principal suppliers. Group businesses continuously monitor and carry out due diligence of suppliers through questionnaires, audits and visits. Based on these assessments and the initiatives implemented by the businesses to counter slavery, the Board was assured that slavery is not taking place within the Group and has published a Modern Slavery statement on the steps taken to prevent slavery, which is available on the Company's website.

#### ENVIRONMENTAL

The Group comprises sales and marketing focused businesses which essentially receive products from suppliers and despatch them to customers. The Group's businesses do not operate delivery fleets; they use third-party carriers to deliver their products to customers and to provide much of their packaging requirements. The Group's ability to control the environmental impact of its logistics partners is therefore limited. The primary impact on the environment, which is entirely in the Group's control, is consumption of the normal business energy sources such as heating and power, which the Group aims to minimise through compliance with relevant environmental legislation.

The Group is committed to identifying and assessing environmental risks, such as packaging waste, arising from its operations. Waste management initiatives are encouraged and supported by the Group and materials are recycled where practical. The Group's usage of water is minimal and relates to cleaning, bathrooms and staff refreshments.

Local management are committed to good environmental management practices throughout our operations. The Managing Directors have responsibility for environmental performance of their operating businesses and each subsidiary is required to implement initiatives to meet their responsibilities.

Each facility participates in recycling paper, plastic, cardboard and wood from pallets and continues to focus on minimising energy consumption through the efficient use of heating and lighting. In addition, a number of the businesses now use fully recycled and biodegradable filler materials for packaging.

#### GREENHOUSE GAS EMISSIONS

UK listed companies are required to report their global levels of Greenhouse Gas ("GHG") emissions in their Annual Report & Accounts. This requirement is for disclosure of Scope 1 and 2 only (direct emissions e.g. heating, cooling, transport fuel; and indirect emissions, e.g. from purchased electricity) and only to the extent that such emissions are the responsibility of the Company.

The Group has considered the six main GHGs and report emissions in tonnes of CO<sub>2</sub> equivalent ("CO<sub>2</sub>e") for Scope 1 (direct) and Scope 2 (indirect) emissions. These emissions are calculated following the GHG Protocol and UK Government Environmental Reporting Guidelines. The Group has used Defra UK GHG Conversion Factors, US Environmental Protection Agency Emission Factors and International Energy Agency Factors.

As a distributor with no owned logistics or freight, the Group's primary direct energy usage and related CO<sub>2</sub> emissions arise from the Group's facilities. Where possible the Group has reported billed data which represents ca. 80% of the Group's global emissions. For the remaining entities the Group has used an estimation using sales data and local conversion factors.

An intensity ratio of CO<sub>2</sub>e per £1m revenue has been selected, which will allow a comparison of performance over time and with other similar types of business.

Source of emissions	Tonnes of CO <sub>2</sub> e	
	2018	2017
Direct emissions (Scope 1)		
Natural gas	726	657
Owned transport	65	68
Indirect emissions (Scope 2)		
Electricity	2,682	2,955
Gross emissions	3,473	3,680
Tonnes CO <sub>2</sub> e per £1m revenue	7.2	8.1

#### TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES ("TCFD")

In June 2017 the TCFD published a voluntary framework to encourage businesses to disclose climate-related risks.

As part of the Group's annual risk management process the Group's businesses consider climate-related risk and where significant, reports these to the Board for review and monitoring. The broad geographic and industrial sector spread of the Group's businesses provide a high degree of resilience to climate-related risks.

The Board has identified that in the shorter term the principal risk from climate change on the Group's businesses arises from extreme weather events that may significantly impact our facilities. In particular the North American Seals Aftermarket business is almost wholly reliant on its central warehouse located in Tampa, Florida. This geography is exposed to hurricanes, generally during the period from August to November each year.

In addition, a significant increase in energy costs caused by carbon taxation, regulation or limited resource would lead to higher costs from external freight and handling costs of delivering product to, or from our facilities.

#### BUSINESS ETHICS

The Group recognises its obligations towards the parties with whom the Group has business dealings including customers, shareholders, employers, suppliers and advisors.

In general, the interactions with these parties are managed at a local level by senior management and the Group expects a high standard of expertise and business principles to be maintained in such dealings.

The Group's policy towards suppliers is that each operating business is responsible for negotiating the terms and conditions under which they trade with their suppliers. The Group does not operate a formal code that it follows with regard to payments to suppliers. Group companies agree payment terms with their suppliers when they enter into binding purchasing contracts for the supply of goods or services. Suppliers are, in that way, made aware of these terms. Group companies seek to abide by these payment terms when they are satisfied that the supplier has provided the goods or services in accordance with the agreed terms and conditions.

#### COMMUNITY

The Group believes that good community relations are important to the long term development and sustainability of the operating businesses.

The Group's businesses participate within their local communities on a number of charitable and fundraising activities primarily in support of health and children's charities.

The Group also contributes to local worthwhile causes and charities and in 2018 the Group made donations to charitable organisations of £47,221 (2017: £54,418). No political donations were made.

# BOARD OF DIRECTORS

## JOHN NICHOLAS<sup>3</sup> Chairman

### Appointed

Joined the Board on 1 June 2013 and appointed Chairman on 21 January 2015. Following the departure of Richard Ingram as Chief Executive Officer on 28 August 2018, John Nicholas was appointed interim Executive Chairman.

### Skills and experience

A Chartered Certified Accountant with a Masters degree in Business Administration from Kingston University, London. John has a wealth of business and commercial experience and spent much of his early career in technology-focused international manufacturing and service companies involved in analytical instruments, fire protection and food processing.

He has been Group Finance Director of Kidde plc (on its demerger from Williams Holdings) and of Tate & Lyle PLC.

### External appointments

John is non-Executive Chairman of Porvair plc.

## NIGEL LINGWOOD Group Finance Director

### Appointed

Joined the Company in June 2001 and appointed Group Finance Director in July 2001.

### Skills and experience

Prior to joining the Company, Nigel was the Group Financial Controller at Unigate PLC where he gained experience of working in a large multinational environment and on a number of large corporate transactions. Nigel qualified as a Chartered Accountant with Price Waterhouse, London.

### External appointments

None.

## CHARLES PACKSHAW<sup>1,2,3</sup> Senior Independent Non-Executive Director

### Appointed

Joined the Board on 1 June 2013 and appointed Senior Independent Director on 27 February 2015.

### Skills and experience

Charles has over 30 years of City experience, including 15 years at HSBC where he was Head of UK Advisory and Managing Director in HSBC's global banking business. Prior to that, he was Head of Corporate Finance at Lazard in London. Charles has been a non-Executive Director of two listed companies and he is also a Chartered Engineer.

### External appointments

Charles is Senior Independent non-Executive Director of BMT Group Limited, non-Executive Director at Fram Farmers Limited and Chair of Prostate Cancer UK.

## EXECUTIVE MANAGEMENT COMMITTEE

### JOHN NICHOLAS Chairman

### NIGEL LINGWOOD Group Finance Director

### STUART BELL

Joined the Group in May 2013 in the Group Finance department, became Group Financial Controller in June 2015 and appointed as Finance Director, International Seals in October 2018.

### DAN BROWN

Joined the Group in October 2015 to take responsibility for the Group's Healthcare businesses across all international markets. Now responsible for the Life Sciences Sector.

### DARIN CLAUSE

Joined the Group in November 2015 to take responsibility for the Seals businesses in North America and more broadly to develop new opportunities in US Industrial Distribution. Now responsible for the Seals Sector.

**ANDY SMITH<sup>1,2,3</sup>**  
**Non-Executive Director**

**Appointed**  
Joined the Board and appointed Chairman of the Remuneration Committee on 9 February 2015.

**Skills and experience**

Andy is Managing Director, Severn Trent Business Services with responsibility for the company's non-regulated businesses. He has many years of plc Board level experience having previously served on the Boards of The Boots Company PLC as Group HR Director and Severn Trent PLC as Water Services Director. Andy is a Mechanical Engineering graduate and has significant operational and HR experience. He has worked in the UK and overseas previously with global businesses including BP, Mars and Pepsi.

**External appointments**  
None.

**ANNE THORBURN<sup>1,2,3</sup>**  
**Non-Executive Director**

**Appointed**  
Joined the Board on 7 September 2015 and appointed Chairman of the Audit Committee on 17 November 2015.

**Skills and experience**

Anne was Chief Financial Officer of Exova Group plc and has many years of experience at Board level in listed international groups. Anne was previously Group Finance Director at British Polythene Industries PLC. Anne is a member of the Institute of Chartered Accountants in Scotland.

**External appointments**  
Anne is a non-Executive Director of BTG plc.

**Director Changes During the Year**

**Bruce Thompson**  
Appointed Chief Executive Officer in 1996 and retired from the Board on 8 May 2018.

**Richard Ingram**  
Joined the Board on 23 April 2018 and appointed Chief Executive Officer on 8 May 2018. Stood down as Chief Executive Officer and as Executive Director on 28 August 2018.

**Committee membership**  
1 Remuneration Committee  
2 Audit Committee  
3 Nomination Committee

**CAROLYN DICK**

Joined the Group in August 2003 in the Group Finance department. Appointed Group FP&A Director in June 2015 with responsibility for the Group's management reporting system and appointed as Group FP&IS Director in October 2018 responsible for the Group-wide Information Systems.

**GUSTAV RÖBER**

Joined the Group in September 2004 initially as Group Financial Controller and appointed Corporate Development Director in 2012. Now responsible for the Controls Sector.

**NEIL YAZDANI**

Neil is currently a Director at Deloitte LLP and will join the Group in January 2019 as Group Financial Controller.

## CORPORATE GOVERNANCE

// WITH A PROVEN STRATEGY  
AND THE SUPPORT OF AN EXPERIENCED  
GROUP OF MANAGERS ON THE EMC,  
THE BOARD IS CONFIDENT THAT IT  
REMAINS IN A STRONG POSITION TO MEET  
THE LIKELY CHALLENGES DURING THIS  
TRANSITION YEAR //

John Nicholas, Chairman

Members of Board	Attendance
<b>Chairman</b>	
John Nicholas	10/10
<b>Independent non-Executive Directors</b>	
Andy Smith	10/10
Charles Packshaw	10/10
Anne Thorburn	9/10
<b>Executive Directors</b>	
Nigel Lingwood	10/10
Bruce Thompson (retired on 8 May 2018)	4/5
Richard Ingram (23 April 2018 to 28 August 2018)	3/3

### DEAR SHAREHOLDER

The Board and its Committees have had a busy year in 2018. At the start of the year, the Nomination Committee was focused on the recruitment of a new CEO to succeed Bruce Thompson. That process concluded in January 2018 with the announcement that Richard Ingram would join the Group in the Spring. I reported last year that the Board recognised that the period of transition to a new CEO was likely to be challenging but I had not anticipated that these challenges would lead to Richard being asked to leave the Group at the end of August. The Committee is again conducting a search for a suitable successor and is working with a different search firm with a revised specification. In the interim, my colleagues have asked me to assume the role of interim Executive Chairman which I have agreed to do.

The Board also reviewed the appropriateness and future potential of the Group's strategy during the year. The current strategy has proven to be resilient and successful over several years and the Board had no hesitation in confirming continued support.

Membership of the Executive Management Committee has recently been broadened to reflect the future requirements of the Group, further appointments, including that of an HR professional are planned for this year. Details of the Committee are set out on pages 36 and 37.

The Remuneration Committee has also spent considerable time on CEO succession matters relating to the recruitment of Richard Ingram and then after the year end in relation to the financial settlement when he departed the Group. Further details of this work are included in the Committee report on pages 56 and 57.

2018 has been the first year for the new Group auditor, PricewaterhouseCoopers ("PwC") and the Audit Committee has worked closely with both PwC and the Group's finance departments to ensure a smooth transition from Deloitte LLP and an effective audit. Further details of this work are in the Committee report on pages 44 and 45.

In line with the UK Corporate Governance Code, the Board held an externally facilitated evaluation towards the end of this year. The review was facilitated by Clare Chalmers leading to a report on her observations which in October was discussed by the Board. I am pleased to report that this report confirmed that the Board and Committees were operating effectively, but I recognise there is always scope for improvement. I am working with the Company Secretary on the suggestions arising from the report and will report on progress next year.

John Nicholas  
19 November 2018



## FRAMEWORK OF CORPORATE GOVERNANCE

### THE BOARD

The Diploma PLC Board is accountable to the Company's shareholders for standards of Governance across the Group's businesses. Certain strategic decision-making powers and authorities of the Company are reserved as matters for the Board. The principal matters reserved for the Board are set out below. Day-to-day operational decisions are managed by the Chief Executive Officer.

- Setting the overall strategic direction and oversight of the management of Diploma PLC.
- Recommending or declaring dividends.
- Approval of the Group and Company financial statements.
- Approval of new bank facilities, or significant changes to existing facilities.
- Assessment and approval of the principal risks facing the Group and how they are being managed.
- Approval of the Viability Statement.
- Maintaining sound internal control and risk management systems.
- Approval of major corporate transactions and commitments.
- Succession planning and appointments to the Board.
- Review of the Group's overall corporate governance arrangements and reviewing the performance of the Board and its Committees annually.
- Approval of the delegation of authority between the Chairman and the Chief Executive Officer and the terms of reference of all Committees of the Board.

Where appropriate, matters are delegated to a Committee, which will consider them in accordance with its terms of reference. Details of each Committee's terms of reference are available on the Diploma PLC website at [www.diplomaplc.com/governance/constitutional-documents](http://www.diplomaplc.com/governance/constitutional-documents).

### AUDIT COMMITTEE

**Chaired by Anne Thorburn**

Number of meetings in the year: five

#### Role of the Committee

The Audit Committee has responsibility for overseeing and monitoring the Company's financial statements, accounting processes, audit (internal and external), internal control systems and risk management procedures and also monitors issues relating to fraud, anti-bribery and corruption, sanctions and whistleblowing.

### NOMINATION COMMITTEE

**Chaired by John Nicholas**

Number of meetings in the year: four

#### Role of the Committee

The Nomination Committee regularly reviews the structure, size and composition of the Board and its Committees. It identifies and nominates suitable candidates to be appointed to the Board (subject to Board approval) and considers succession generally.

### REMUNERATION COMMITTEE

**Chaired by Andy Smith**

Number of meetings in the year: six

#### Role of the Committee

The Committee reviews and recommends to the Board, the framework and policy for the remuneration of the Chairman and the Executive Directors. The remuneration of the non-Executive Directors is determined by the Chairman and the Executive Directors. The Committee takes into account the business strategy of the Group and how remuneration policy should reflect and support that strategy.

### LEADERSHIP

#### Board composition

The Board comprises a Chairman, one Executive Director and three independent non-Executive Directors. The non-Executive Directors are appointed for specified terms and the details of their respective appointments are set out in the Remuneration Committee Report on page 55. The biographical details of the Board members are set out on pages 36 and 37.

John Nicholas is Chairman of the Board and Chairman of the Nomination Committee. Each of the three independent non-Executive Directors performs additional roles: Charles Packshaw serves as Senior Independent Director, Andy Smith is Chairman of the Remuneration Committee and Anne Thorburn is Chair of the Audit Committee.

#### Activities of the Board

The Company's governance framework is set out above together with a summary of the formal terms of reference. The core activities of the Board and its Committees are planned on an annual basis and this framework forms the basic structure within which the Board operates.

The Board's terms of reference also set out the separate and distinct roles of the Chairman and the Chief Executive Officer.

## COMPLIANCE WITH THE CODE

Diploma PLC is required to state how it has applied the Main Principles of the UK Corporate Governance Code ("the Code"), issued by the Financial Reporting Council in April 2016. Set out on pages 40 to 42 is an explanation of how the Company has applied the Main Principles of the 2016 Code.

The Board confirms that throughout the financial year, the Company applied all of the Principles set out in sections A to E of the Code for the period under review. The Board also confirms that it complies with all of the Provisions of the Code, with the single exception of A.2.1 as explained below:

The Code requires that the role of Chairman and Chief Executive Officer should not be exercised by the same individual. While this is ordinarily the case for the Company, following the departure of Richard Ingram, Chief Executive Officer, on 28 August 2018, the Board appointed John Nicholas as interim Executive Chairman until a new Chief Executive Officer is appointed. The Nomination

Committee has appointed an external search agency to assist the Board with the appointment of a new Chief Executive Officer. On appointment of a new Chief Executive Officer, John Nicholas will relinquish his role as interim Executive Chairman and revert to his previous role as non-Executive Chairman.

The Company's auditor PricewaterhouseCoopers LLP, is required to review whether this statement reflects the Company's compliance with the Provisions of the Code specified for their review by the Listing Rules of the FCA and to report if it does not reflect such compliance.

In July 2018, the FRC issued a new Code which will be mandatory for the Company in respect of the year ending September 2020. The Board will assess its governance practices against the provisions of the new Code during 2019 and will report on its implementation in next year's Annual Report & Accounts.

## CORPORATE GOVERNANCE CONTINUED

The Chairman is responsible for the overall leadership and governance of the Board and ensures that the Directors have an understanding of the views of the Company's major shareholders. The Chairman sets the Board's agenda and ensures that there is a healthy culture of challenge and debate at Board and Committee meetings.

The Board appoints the Chief Executive Officer and monitors their performance in leading the Company and providing operational and performance management in delivering the agreed strategy. The Chief Executive Officer is responsible for developing, for the Board's approval, appropriate values, culture and standards to guide all activities undertaken by the Company and for maintaining good relationships and communications with investors.

The approval of acquisitions, for the most part, is a matter reserved for the Board, save that it delegates to the Chief Executive Officer the responsibility for such activities to a specified level of authority. Similarly, there are authority levels covering capital expenditure that can be exercised by the Chief Executive Officer. Beyond these levels of authority, projects are referred to the Board for approval.

Other matters reserved to the Board include treasury policies, internal control and risk management.

To ensure that non-Executive Directors can constructively challenge and support proposals on strategy, the Board has adopted a process of reviewing and approving the agreed strategy for the Company on a three-yearly basis. The Board met in October 2018 and reviewed an update of the Company's strategy. A more structured and formal review will be undertaken by a new Chief Executive Officer, in the year following appointment.

### Meetings of the Board

The Board has seven scheduled meetings during the financial year but will meet more frequently if required. In 2018 the Board had an additional three meetings largely as a consequence of matters relating to the appointment and subsequent departure of the Chief Executive Officer.

Each Director is expected to attend all meetings of the Board or Committees of which they are a member. In addition, senior management from across the Group and advisors attend certain meetings for the discussion of specific items in greater depth.

Bruce Thompson and Anne Thorburn were unable to attend the Board meeting on 11 December 2017 and 25 September 2018, respectively. Both meetings were called at short notice.

The Board ensures that at least one of the scheduled meetings is held on site at one of the Group's facilities, where the Board has an opportunity to both receive presentations from local management and meet employees of that business. In August 2018, the Board's scheduled meeting was held at Cablecraft's facility in Houghton Regis, UK. At this meeting the Board received presentations from senior management in Cablecraft and had an opportunity to view the facility and meet with employees to gain a better understanding of the products and operations managed from this facility.

In October 2018, the Board approved a report on an update of the Group's strategic objectives for the three years ending 30 September 2021. This report was prepared on a top down basis with substantial input from the Executive Management Committee ("EMC") and supported by a detailed financial model which was used to assess different scenarios over the strategy period. As part of this exercise members of the EMC met for two days in London in July 2018 to review their business strategy and the opportunities to develop their Sectors, including their acquisition strategy. Based on the output from this meeting, a report was prepared by the interim Executive Chairman and Group Finance Director and was presented to and approved by the Board on 2 October 2018.

### EFFECTIVENESS

#### Independent non-Executive Directors

The non-Executive Directors are determined by the Board to be independent in character and judgement and there are no relationships or circumstances that could affect, or appear to affect, a Director's judgement. The Chairman, John Nicholas was considered independent by the Board both at the time of his appointment as Director on 1 June 2013 and as Chairman on 21 January 2015. John Nicholas was appointed interim Executive Chairman on 28 August 2018 following the departure of Richard Ingram, Chief Executive Officer, until a permanent Chief Executive Officer is appointed.

All non-Executive Directors are advised of the likely time commitments at appointment. The ability of individual Directors to allocate sufficient time to the discharge of their responsibilities is considered as part of the Directors' annual evaluation process, overseen by the Chairman. Any issues concerning the Chairman's time commitment are dealt with by the Nomination Committee, chaired for this purpose by the Senior Independent Director.

Each non-Executive Director is required to inform the Board of any changes to their other appointments.

During the year, the Chairman has also held meetings with the non-Executive Directors, without the Executive Directors present.

The appointment of non-Executive Directors are subject to formal, rigorous and transparent procedures which are described more fully in the Nomination Committee Report which is set out on page 48.

#### Diversity

The Board is committed to a culture of equal opportunity and diversity to attract and retain talented people to deliver outstanding performance and further enhance the success of the Group.

In that culture, diversity across a wide range of criteria is valued, including skills, knowledge and experience as well as gender, ethnicity, religion and sexual orientation. People are appointed on merit, in an equal opportunities environment and without any form of positive or negative discrimination. External consultants, when used, are made aware of this policy.

The Nomination Committee reviews the structure, size, diversity, balance and composition of the Board and makes recommendations to the Board concerning the reappointment of any non-Executive Director at the conclusion of their specified term of office and in the identification and nomination of new Directors. The principal objective of the Nomination Committee is to ensure that all candidates have appropriate knowledge, ability and experience for the role.

The Board supports the recommendations of the Hampton-Alexander review on gender diversity but believes that other types of diversity are equally important. The Board is currently diverse across a range of criteria, but it is committed to strengthen that diversity, including gender and ethnic diversity, when appropriate opportunities arise. The Board will also take account of its objective to meet the Hampton-Alexander review targets before the end of the next Board rotation of non-Executive Directors. Additional information on diversity can be found on page 34.

### Information and professional development

An induction programme is agreed for all new Directors aimed at ensuring that they are able to develop an understanding and awareness of the Group's core processes, its people and businesses. The non-Executive Directors' awareness of the businesses is further developed through periodic visits to the principal business locations and presentations to the Board by senior management of the businesses. In 2018, the Board received presentations from senior management of the Cablecraft business.

Following a new appointment to the Board, a managed induction programme is arranged that includes a visit by the Director to the major business units in each of the Group's Sectors where they have an opportunity to meet with senior management in these businesses. Meetings are also held individually between each of the non-Executive Directors and the Executive Directors and with some of the principal advisors to the Company. A managed and thorough induction programme was also arranged following the appointment of the Chief Executive Officer in May 2018. This programme provided for one-to-one meetings with members of the Board, members of the EMC and key advisors to the Company, together with substantive visits to the Group's principal businesses.

The Chairman, with the assistance of the Chief Executive Officer and the Group Company Secretary, is responsible for ensuring that Directors are supplied with information in a timely manner that is in a form and of a quality appropriate to enable them to discharge their duties. In the normal course of business, the Chief Executive Officer gives an oral report to the Board at each meeting and information is provided and reported through formal Board reports that include information on operational matters and strategic developments. There are also reports on the performance of the Group's businesses, financial performance relative to the budget, risk management, business development and investor relations.

The training needs of the Directors are periodically discussed at Board meetings and where appropriate, briefings as necessary are provided on various elements of corporate governance and other regulatory issues.

The Chairman has reviewed and agreed the training and development needs of individual Directors and encourages them to continually update their skills, together with knowledge and familiarity with the Company to fulfil their role on the Board and Board Committees.

The Group Company Secretary acts as an advisor to the Board on matters concerning governance and regulatory issues and ensures compliance with Board procedures. All Directors have access to his advice. The appointment and removal of the Group Company Secretary and his remuneration are matters for the Board as a whole.

### Board evaluation

The Board undertakes an externally led evaluation of the effectiveness of the Board every three years, in accordance with the Code. This exercise encompasses an evaluation of the Board as a whole, the Board Committees and of individual Directors of the Company.

The most recent evaluation was carried out in August 2018 and was externally led by Clare Chalmers, who had no other connection with the Company. The external facilitator interviewed all Directors who had served during the year, with the exception of Richard Ingram who had stepped down from his role as Chief Executive Officer and as a Director of the Company, together with the Group Company Secretary. The evaluation also included a review of the Annual Report & Accounts, with particular focus on the section on corporate governance. There was also a review of the Board and Committee meeting papers, including minutes of each meeting.

A written report was provided to all Board members that concluded that the Board had a collegiate culture led by a capable and experienced Chairman; it added that there were sound governance and Board processes, with a successful and well-supported remuneration policy and that there was good and detailed financial reporting.

The report also set out 16 suggestions for the Board to consider relating to Board Dynamics and Culture, Board and Executive Skills and Succession, Strategic Focus, Communication & Stakeholders, Risk, Committees and Information Quality and Board Papers.

The Board met in early October to discuss the report and Clare Chalmers was invited to the meeting to facilitate an in-depth discussion of these sixteen suggestions. Following this meeting, the Chairman and the Group Company Secretary were tasked with producing an action list and timetable for the Board to implement the salient recommendations, details and progress against which will be reported on in next year's Annual Report & Accounts.

In those years when an external evaluation is not performed, the Board undertakes an internal evaluation of the Board's effectiveness using specially designed evaluation forms under the direction of the Chairman. This exercise encompasses an evaluation of the performance of the Board as a whole, as well as of each of the Committees and individuals. Feedback on Board performance is presented by the Chairman to the Board and actions and objectives are agreed for the following year.

The Senior Independent Director, together with the non-Executive Directors also carries out each year (and has done so in 2018), a performance evaluation of the Chairman, having taken account of the views of all of the Directors.

### Re-election

All Directors of the Board are subject to election by the shareholders at the first AGM following their appointment by the Board and in accordance with the Code, all Directors will also stand for re-election annually at the AGM.

### Liability insurance

In line with market practice, each Director is covered by appropriate Directors' and Officers' liability insurance ("D&O"), at the Company's expense. The D&O insurance covers the Directors and Officers against the costs of defending themselves in legal proceedings taken against them in that capacity and in respect of any damages resulting from those proceedings. The Company also indemnifies its Directors and Officers to the extent permitted by law. Neither the insurance nor the indemnity provides cover where the Director or Officer has acted fraudulently or dishonestly.

### Professional advice

A policy is in place pursuant to which each Director may obtain independent professional advice at the Company's expense in furtherance of their duties as a Director of Diploma PLC. No formal requests were made during the year, but post-year end, advice was sought in relation to Board succession. In addition, each of the Committees are authorised, through their Terms of Reference, to seek advice at the Company's expense. During the year substantial advice was sought by the Chairman of the Remuneration Committee in relation to the appointment and subsequent financial settlement in connection with the departure of the Chief Executive Officer.

## CORPORATE GOVERNANCE CONTINUED

### Conflicts of interest

Directors are subject to a statutory duty under the Companies Act 2006 ("the Act") to avoid a situation where they have, or could have, a direct or indirect interest that conflicts, or possibly could conflict, with the Company's interests. The Act allows directors of public companies to authorise conflicts and potential conflicts where appropriate, where the Articles of Association ("the Articles") contain a provision to this effect. The Act also allows the Articles to contain other provisions for dealing with Directors' conflicts of interest to avoid a breach of duty.

Procedures adopted to deal with conflicts of interest continue to operate effectively and the Board's authorisation powers are being exercised properly in accordance with the Company's Articles.

### ACCOUNTABILITY

The Board is responsible for ensuring that the Annual Report & Accounts taken as a whole present a fair, balanced and understandable assessment of the Group and provides the information necessary to shareholders to assess the Group's position and performance, business model and strategy. The Board receives a detailed Report from the Group Finance Director which sets out the key matters that impact, or could impact the Group's financial statements and Annual Report and highlights areas of the financial statements where it has been necessary to rely upon a significant level of subjectivity. The Board also has access to all relevant information and reviews other periodic management information and RNS announcements. The draft Annual Report & Accounts are circulated to each member of the Board in sufficient time to allow challenge of the disclosures where necessary. The Directors' responsibilities statement is set out on page 65.

The Board is responsible for determining the nature and extent of the principal risks it is willing to take in achieving its strategic objectives and for maintaining sound risk management and internal control systems. The Board is also responsible for monitoring the Group's risk management and internal control systems and it reviews the effectiveness of these systems through the work of the Audit Committee.

The principal risks which the Board has identified this year are set out in the section on Internal Control and Risk Management on pages 30 to 33 of the Strategic Report.

### RELATIONS WITH SHAREHOLDERS

The Company has a well-developed investor relations programme managed by the Chief Executive Officer and Group Finance Director, with the support of the Company's brokers. Through this programme, the Company maintains regular contact with major shareholders to communicate clearly the Group's objectives and monitors movements in significant shareholdings.

In addition, Investor Roadshows are now held each year in the US and Canada as well as in the UK and formal investor presentations are made twice a year to groups of private client fund managers. The Company also engages with existing and potential new investors through a formal Capital Markets Day at which attendees have an opportunity to meet with senior management in the Group to gain a better understanding of the businesses' product portfolios. The last Capital Markets Day was held in February 2017 in London.

Most shareholder contact is with the Chief Executive Officer and Group Finance Director through presentations made twice a year on the operating and financial performance of the Group and its longer term strategy. The Chief Executive Officer and Group Finance Director generally deal with questions from individual shareholders.

The Group's website contains up-to-date information for shareholders, which includes the Annual Report & Accounts of the past ten years, current and historic share price information, news releases and presentations to analysts and key shareholders. The website also contains factual data on the Group's businesses, products and services.

The non-Executive Directors are given regular updates as to the views of institutional shareholders and independent insight is sought through research carried out twice a year by the Company's advisors, focused on both investors and analysts.

Through these processes, the Board is kept abreast of key issues and the opportunity is available on request for shareholders to meet the Chairman or Senior Independent Director, separately from the Executive Directors.

Electronic communications to shareholders include the Notice of the AGM, which is sent at least 20 working days prior to the meeting. The Company proposes a separate resolution on each separate issue and for each resolution, proxy appointment forms provide shareholders with the option to vote in advance of the AGM.

All shareholders have the opportunity to put questions at the Company's AGM, when the Chairman and Chief Executive Officer give a statement on the Group's performance during the year, together with a statement on current trading conditions. The Chairman of the Board and of the Remuneration and Audit Committees are available to answer questions at the meeting.

The Board has resolved, in line with best practice, to conduct a poll on each resolution proposed at the AGM. The results of the AGM resolutions, including details of votes cast, are published on the Company's website.

With regard to shareholder meetings, other than AGMs, the Board will continue, in ordinary circumstances, to provide as much notice as possible and certainly no less than 14 working days. However, the Board considers that it should still retain the flexibility to reduce the timescale to 14 clear days in the case of non-routine business and where it is merited by the business of the meeting. For this reason, the Board has again proposed a resolution at the AGM to reduce the notice period for General Meetings from 21 to no less than 14 clear days.

## AUDIT COMMITTEE REPORT

**“ THE GROUP CONTINUES TO MAINTAIN  
A CULTURE OF ROBUST AND EFFECTIVE  
SYSTEMS OF INTERNAL CONTROL,  
OVERSEEN BY STRONG AND EXPERIENCED  
FINANCE DEPARTMENTS ”**

Anne Thorburn, Chairman of the Audit Committee

Members of Committee	Attendance
Anne Thorburn (Chairman)	5/5
Charles Packshaw	5/5
Andy Smith	5/5

### DEAR SHAREHOLDER

The Committee welcomed Christopher Burns of PwC to the Company as the new auditor this year, following the formal appointment at the AGM of PwC as auditor to the Company after a competitive tender process last year. After attending last year's audit close meeting, alongside the retiring auditor, they worked diligently during the first half of the year to complete their audit transition process. At the close of this process PwC met with the Committee to confirm that they had completed their handover with the retiring auditor, had met with senior finance staff across the business and they had no significant concerns to bring to the Committee's attention.

In March this year, the Committee received a report from the Group finance team that set out a detailed evaluation of the potential impact that the new IFRS15 standard on Revenue may have on the Group's financial statements. The report was based on detailed discussions that the Group finance team had with each of the individual businesses. As expected, given the nature of the Group's business, this work confirmed that the impact on the financial statements from adopting IFRS15 was negligible. A similar exercise will be carried out in 2019 to assess the potential impact of adopting IFRS16 on Leases, and it is likely that the impact on the financial statements may be significant, as explained further on page 93 in the notes to the consolidated financial statements.

The Committee was pleased to welcome during the year the appointment of an experienced tax professional as Head of Group Tax & Treasury. The tax environment and tax demands on business have become increasingly more complex in recent years, particularly where the Group has significant operations based outside the UK. This appointment will ensure that the Group businesses both maintain compliance with local tax legislation and focus on good tax governance.

I also look forward to Neil Yazdani joining the Group in January 2019 as Group Financial Controller. Neil will replace Stuart Bell who has now moved to International Seals to support Darin Clause as Finance Director of those businesses.

As Chairman of the Committee, I continue to meet regularly with members of the Internal Audit team to discuss their reports, prepared following each of their visits to the businesses. This provides me with greater insight of the culture of the internal control environment in the Group and provides assurance that controls are both in place and are tested, which is particularly important given the Group's decentralised operating model.

I am pleased to report that again there have been no significant control deficiencies or accounting irregularities reported to the Committee this year. The Group continues to maintain a culture of robust and effective systems of internal control, overseen by strong and experienced finance departments.

I look forward to meeting shareholders at the AGM on 16 January 2019 and will be happy to respond to any questions relating to the activities of the Audit Committee.

Anne Thorburn  
19 November 2018

## AUDIT COMMITTEE REPORT CONTINUED

### KEY DUTIES AND FOCUS IN 2018

The Audit Committee is responsible for ensuring that the Company maintains a strong control environment. It provides effective governance over the Group's financial reporting, including oversight and review of the systems of internal control and risk management, the performance of internal and external audit functions, as well as the behaviours expected of Diploma PLC's employees through the whistleblowing policy and similar codes of conduct. The Committee's role and responsibilities are set out in its Terms of Reference, which are reviewed every two years and are approved by the Board.

The Terms of Reference are available at [www.diplomapl.com/governance/constitutional-documents](http://www.diplomapl.com/governance/constitutional-documents). The Committee's key responsibilities and focus during the year have been:

- Reviewed and agreed the scope of audit work to be undertaken by the external auditor and agreed the terms of engagement and fees to be paid for the external audit.
- Reviewed the Annual Report & Accounts and received reports from the Group Finance Director and the external auditor on the key accounting issues and areas of significant judgement.
- Reviewed the report on compliance with the UK corporate governance Code and reports on the provision of information to the auditor.
- Reviewed the report from the Group Finance Director on the controls in place to mitigate fraud risk.
- Reviewed the Half Year Announcement and received reports from the Group Finance Director and the external auditor on the key accounting issues and areas of significant judgement.
- Reviewed a report from the Group finance department setting out the impact of new IFRSs on the Group's financial statements, including in particular IFRS15 (revenue from contracts with customers).
- Reviewed and approved the classification and presentation of the costs incurred on the CEO transition.
- Reviewed the Trading Updates at meetings held in January, March and August.
- Reviewed the effectiveness of the Group's internal control and risk management procedures and, where appropriate, made recommendations to the Board on areas for improvement.
- Invited the Director of Internal Audit to attend meetings to review the results of the Internal Audit work for the current year and to agree the scope and focus of Internal Audit work to be carried out in the following year.
- Reviewed the transition to PwC following their appointment as the Group's external auditor.
- Approved the Committee work programme for 2018.
- Reviewed the scope of new sanctions issued by the European Union and the US and the procedures being followed by the Group's businesses to monitor compliance.
- Reviewed the whistleblowing arrangements and the use of a dedicated external independent and confidential telephone hotline service for all employees to raise concerns.

### AUDIT COMMITTEE

The Committee is chaired by Anne Thorburn and comprises three independent non-Executive Directors. The Chair of the Committee is a qualified accountant, who has recent and relevant financial experience.

The Audit Committee is satisfied that as a whole, the Committee has sufficient knowledge and competence of the business model and Sectors in which the Group operates in order to provide appropriate challenge to management.

The Group Company Secretary acts as Secretary to the Committee. The Executive Directors also attend Committee meetings and the Internal Audit Director also attended Committee meetings to present the Internal Audit plan for the following year and to report on progress against that plan. The Committee met with the external auditor during the year, without the Executive Directors being present.

The Audit Committee confirms that the Company has complied with the provisions of the Competition & Markets Authority Order throughout its financial year ended 30 September 2018 and up to the date of this report.

### AUDIT TRANSITION

The Audit Committee completed an audit tender process in 2017 (as described more fully in the Annual Report & Accounts 2017) and recommended to the Board the appointment of Christopher Burns, PricewaterhouseCoopers LLP ("PwC") as auditor. The Board accepted and endorsed this recommendation, which was approved by shareholders at the AGM held on 17 January 2018.

The Audit Committee agreed an audit transition plan with PwC which identified key milestones, beginning with PwC shadowing Deloitte LLP ("Deloitte"), the retiring auditor, at the 2017 Group audit close meeting with management and the Audit Committee meeting held on 14 November 2017. During the first half of this year, PwC met with both members of the Group finance department and senior finance personnel of the larger businesses in the Group. At these meetings, work was carried out by PwC to plan their audit approach and prepare their audit strategy for the 2018 audit. In May, PwC reported to the Audit Committee that they had completed their audit transition plan and that there were no substantive matters to report to the Committee.

## ENGAGEMENT OF THE EXTERNAL AUDITOR

The external auditor is engaged to express an opinion on the financial statements of the Group and of the Company. The audit includes the review and testing of the systems of internal financial control and the data contained in the financial statements, to the extent necessary for expressing an audit opinion on the truth and fairness of the financial statements.

As explained above, the Company's Annual Report & Accounts this year has been audited by PwC. In their first year as auditor, PwC has met with the Audit Chair and has agreed its audit strategy and audit fees with the Audit Committee. As part of its audit, PwC will continue to provide the Committee with relevant reports, reviews and advice throughout the coming year.

In accordance with UK regulations, PwC also assured the Committee that it adheres to a rotation policy based on best practice and the Group engagement partner will serve a period of no longer than five years.

During the year, the Committee carried out an assessment of the effectiveness of the external audit process for the previous year ended 30 September 2017, which was carried out by Deloitte. The assessment was led by the Chair of the Committee, assisted by the Group Finance Director and focused on certain criteria which the Committee considered to be important factors in demonstrating an effective audit process. These factors included the quality of audit staff, the planning and execution of the audit and the role of management in the audit process. Following this assessment, the Committee concluded that the external audit process remained effective and that it provides an appropriate independent challenge of the Group's senior management.

The Committee was satisfied that the Deloitte audit of the Company and Group had provided a robust and effective audit and supported the work of the Committee through clear and objective communication on developments in financial reporting and governance.

## NON-AUDIT SERVICES

The Committee has reviewed the Company's internal guidelines covering the type of non-audit work that can be carried out by the external auditor of the Company, in light of the regulation set out in the EU Audit Directive and Audit Regulation 2014 ("the Regulations").

The Regulations substantially curtail those non-audit services that can be provided by the auditor to the Company and in particular, prohibits all tax related services, including compliance services as well as general advice and all consultancy and advisory services. The Regulations require that Board approval is required if eligible non-audit services, such as due diligence and similar assurance services exceed 30% of the prior year Group audit fee and the Company may not allow eligible non-audit services to exceed 70% of the Group audit fee, calculated on a rolling three-year basis.

The Group Finance Director does not have delegated authority to engage the auditor to carry out any non-audit work, but must seek approval from the Chair of the Audit Committee.

Taxation services are not provided by the Group's current audit firm; a separate firm is retained to provide tax advice and any assistance with tax compliance matters generally. In addition, due diligence exercises on acquisitions and similar transactions are not provided by the auditor, but are placed with other firms.

The Group auditor is retained to carry out assurance services to the Committee in connection with "agreed upon procedures" on the Group's Half Year consolidated financial statements. With the exception of this work, PwC has not provided any non-audit services to the Company or its subsidiaries and has confirmed their independence to the Audit Committee. The fees for carrying out this work comprises the total non-audit fees of £15,000 set out in note 27 to the consolidated financial statements.

The Committee assures itself of the auditor's independence by receiving regular reports from the external auditor which provide details of any assignments and related fees carried out by the auditor in addition to their normal audit work and these are reviewed against the above guidelines. PwC has reconfirmed its independence for the current financial year.

## FINANCIAL REPORTING AND SIGNIFICANT FINANCIAL JUDGEMENTS

As part of its monitoring of the integrity of the financial statements, the Committee reviews whether suitable accounting policies have been adopted and whether management has made appropriate estimates and judgements and seeks support from the external auditor to assess them.

The Committee considered the matters set out below as being significant in the context of the consolidated financial statements for the year ended 30 September 2018. These were discussed and reviewed with management and the external auditor and the Committee challenged judgements and sought clarification where necessary. The Committee received a report from the external auditor on the work they had performed to arrive at their conclusions and discussed in detail all material findings contained within the report.

### Provisions for excess and slow moving inventory

The Committee reviewed the Report of the Group Finance Director that set out the gross balances by business, together with any related provision against the carrying value. The Committee reviewed the bases used to value and confirm existence of inventory held across the Group; they also considered the appropriateness of provisions held against the carrying value of inventory, having regard to the age and volumes of inventory, relative to expected usage. Following their review, which also included consideration of the external audit findings, the Committee concluded that the provision for excess and slow moving inventory is appropriate.

### Impairment of goodwill

The Committee considered the carrying value of goodwill and the assumptions underlying the impairment review. The judgements in relation to goodwill impairment largely relate to the assumptions underlying the calculations of the value in use of the Cash Generating Unit ("CGU") being tested for impairment. These judgements are primarily the calculation of the discount rate, the achievability of management's forecasts in the medium term and the use of the long term growth rate. Following their review which also included consideration of the external audit findings, the Committee concurred with the conclusion that no impairment of goodwill is required.

## AUDIT COMMITTEE REPORT CONTINUED

In addition to the above the Committee also seeks confirmation from the auditor that the Group's businesses follow appropriate policies to recognise material streams of revenue and their audit work carried out more generally has assessed any instances where management may be able to override key internal controls designed to guard against fraud or material misstatement. The auditor also reported to the Committee on other less material matters in relation to the recoverability of trade receivables, acquisition accounting, the valuation of the Group's defined benefit schemes and the classification and presentation of the CEO transition costs.

### CHANGES IN ACCOUNTING STANDARDS

The Audit Committee reviewed the likely impact of adopting IFRS15 (revenue from contracts with customers) ahead of the implementation across the Group, which will be applicable for the year ending 30 September 2019. A report prepared by the Group Finance department on the potential impact of this standard on the Group's consolidated financial statements was submitted to the Committee during the year. This report was based on a detailed review carried out in conjunction with the Heads of Finance of the major businesses. This report identified that the new standard may affect some contracts for bundled goods and services in relation to reagent rental agreements in Diploma Healthcare Group, as well as preventive maintenance service and CEMS revenues in a1-CBISS. The amounts relating to these revenue streams were in aggregate less than 1% of total Group revenues. The bases applied to revenue recognition across the Group will continue to be monitored to ensure compliance with IFRS15.

The Audit Committee also noted initial project work being carried out by the Group Finance department on the impact of IFRS16 (leases) on the Group's consolidated financial statements, which will be applicable for the year ending 30 September 2020. This standard will affect Diploma in that all material operating leases (including properties) will be capitalised on the Balance Sheet and depreciated. The Group Finance department will again report formally in 2019 to the Committee on the potential implications on the consolidated financial statements from adopting this standard.

Further information on the impact of IFRS15 and IFRS16 is set out on pages 92 and 93.

### TAX STRATEGY

The Committee noted that during the year, the Group tax strategy, including detailed tax policies, had been updated by the Head of Tax and Treasury and has been reviewed and approved by the Board.

### RISK MANAGEMENT AND INTERNAL CONTROL

The principal risks and uncertainties that are currently judged to have the most significant impact on the Group's long term performance are set out in a separate section of the Strategic Report on Internal Control and Risk Management on pages 30 to 33.

The Committee is responsible for reviewing the effectiveness of the Group's system of internal control. The system of internal control is 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 Group has the necessary procedures in place to ensure that there is an ongoing process for identifying, evaluating and managing the principal risks to the Group. These procedures are in line with the Financial Reporting Council's guidance.

The Board has established a clear organisational structure with defined authority levels. The day-to-day running of the Group's business is delegated to the Executive Directors of the Company who are supported by members of the Executive Management Committee ("EMC") comprising of the heads of each business Sector and functional heads of Group FP&IS and Group Finance. The EMC and Executive Directors visit each operating unit on a regular basis and meet with both operational and finance management and staff.

Key financial and operational measures relating to revenue, cash and receivables are reported on a weekly basis. Detailed management accounts and KPIs are prepared monthly using a robust proprietary reporting system to collect and analyse financial data in a consistent format. Monthly results are measured against both budget and half year reforecasts which have been approved and reviewed by the Board. All capital expenditure above predefined amounts must be supported by a paper prepared by management.

All financial data is taken directly from the trial balance of each business held in their local ERP systems and reanalysed and formatted in a separate Group management reporting system, operated by the Group finance department. There is no rekeying of financial data and very limited use is made of spreadsheets by the Group businesses to report monthly financial results. The Group finance department continues to develop the functionality of this management reporting system to provide greater insights into the activities of the Group's businesses, both financial and operational. The Group's Internal Auditor regularly audits the base data at each business to ensure it is properly reported through to the Group management reporting system.

As part of the year end close process each business is required to complete a self-assessment that evaluates their financial control environment in their business, which is designed to identify weaknesses in controls. These assessments are critically reviewed by the Group's Director of Internal Audit and a summary for each business is prepared for the Audit Committee. In addition, senior management of each business are required to confirm their adherence with Group accounting policies, processes and systems of internal control by means of a representation letter addressed to the Audit Committee.

The Committee has reviewed the effectiveness of the Group's risk management and internal control systems for the period from 1 October 2017 to the date of this Report. Taking into account the matters set out on pages 30 to 33 relating to principal risks and uncertainties and the reports from the Director of Internal Audit, the Board, with the advice of the Committee, is satisfied that the Group has in place effective risk management and internal control systems.

### INTERNAL AUDIT

The Group maintains a small Internal Audit department which reports directly to both the Group Finance Director and Chair of the Audit Committee. The department comprises a Group Director of Internal Audit, based at one of the Group's businesses in Minneapolis, US and a Group Senior Internal Auditor based at the Group's offices in London.

A full programme of Internal Audit visits has been completed during the year. The scope of work carried out by Internal Audit generally focuses on the internal financial controls and risk management procedures operating within each business, but was expanded this year to include regulatory & compliance reviews and business process improvement. In January, the



Group Director of Internal Audit presented his audit plan for the year to the Committee for their approval. Formal written reports are prepared on the results of each Internal Audit visit that set out internal control weaknesses/risks identified during their work, together with recommendations to improve the internal control environment and mitigate these weaknesses/risks. These reports are discussed with management of the business visited and are reviewed by the appropriate member of the Executive Management Committee.

At the end of the financial year, the Group Director of Internal Audit formally reports to the Committee on the results of the Internal Audit work carried out by his department during the year. The Committee reviews management's responses to matters raised, including the time taken to resolve such matters. The Audit Chair also meets separately with the Group Director of Internal Audit at least twice a year to review some of the department's reports and discuss their findings.

There were no significant or high risk matters identified in the internal audits undertaken during the current financial year. Several recommendations were made to the businesses in regards to implementing adequate and effective internal controls and procedures within the key processes related to their general IT and cybersecurity framework. The Group Director of Internal Audit also reported that good progress has been made with addressing those recommendations made in 2017 in connection with establishing and maintaining adequate segregation of duties within key process areas and more detailed employee expense reporting. It was also identified that further work is still required at some businesses to formalise and improve their inventory cycle count procedures.

The work of the Internal Audit department was also extended this year to review and report on progress made by Group businesses in ensuring that their internal control environment was sufficiently robust to resist cyber-attacks and that businesses have obtained or are seeking to obtain the Cyber-Essentials Basic certification. This work identified a number of instances where systems need to be upgraded and strengthened and these results were reported to the member of the EMC who has been given responsibility for managing and reporting to the Board on the Group's cybersecurity status.

The Internal Audit department also continues to monitor the businesses compliance with Group policies on anti-bribery/corruption and sanctions.

The Committee conducted the annual review of the effectiveness of the Internal Audit department, including its terms of reference, audit plan, general performance and relationship with the external auditors. Based on its review the Committee was satisfied with the effectiveness of the Group's Internal Audit function, specifically the Committee is satisfied that the Internal Audit department is sufficiently independent of Executive management and has sufficient resources and scope that is appropriate for the size and nature of Diploma PLC.

#### SANCTIONS

The Audit Committee continued to work with senior management of the Company, in conjunction with local management of Kentek's Russian operations, to ensure ongoing compliance with EU and US led sanctions. The Committee has received reports on compliance with these sanctions and will continue to monitor developments until the sanctions are suspended or revoked.

#### ANTI-BRIBERY AND CORRUPTION

Diploma PLC maintains a Group-wide policy on anti-bribery/corruption that addresses the requirements of the Bribery Act 2010. The Committee periodically reviews this policy and the procedures to ensure continued and effective compliance in its businesses around the world. During the year, the Group rolled out a refresher using an E-learning training programme to all its business. This training has been undertaken by all senior management and employees in customer or supplier facing roles and in particular by management and employees from companies that have recently joined the Group.

#### WHISTLEBLOWING

The Committee also monitors the Group's whistleblowing policy, which provides the framework to encourage and give employees confidence to "blow the whistle" and report irregularities. The policy, together with hotline posters are placed on site noticeboards across the Group. Employees are encouraged to raise concerns via the confidential multilingual hotline, which is managed by an independent external company and is available 24/7, 365 days a year. Reports to the hotline are investigated and reported to the Committee, together with details of corrective action taken. The Group received three such whistleblowing reports during the year, which on further investigation were found to be personal grievance matters. On further review and investigation, the Committee concluded that two of these reports related to grievance issues in the workplace and the third report comprised concerns that on investigation were not substantiated. All three cases reported to the Committee were satisfactorily resolved.

# NOMINATION COMMITTEE REPORT

Members of Committee	Attendance
John Nicholas (Chairman)	4/4
Charles Packshaw	4/4
Andy Smith	4/4
Anne Thorburn	4/4

The Nomination Committee is chaired by John Nicholas, Chairman of the Company. The Committee is chaired by the Senior Independent Director on any matters concerning the Chairman of the Company. The Committee comprises the non-Executive Directors and meets as necessary to discharge its responsibilities.

The Group Company Secretary acts as Secretary to the Committee.

## RETIREMENT AND APPOINTMENT OF CHIEF EXECUTIVE OFFICER ("CEO")

The Committee has focused this year on the appointment of a new CEO, following the announcement on 26 September 2017 that Bruce Thompson intended to retire as CEO of Diploma PLC during 2018 and leave the Company on 30 September 2018. The recruitment process to appoint a new CEO commenced in the second half of 2017 and was described in last year's Committee report. In summary, a thorough process was undertaken with the assistance of Ridgeway Partners ("Ridgeway"), a search consultancy which did not have any other connections with the Company.

In particular:

- a detailed specification for the role was prepared against which potential candidates were considered;
- Ridgeway provided a long list of potential candidates to the Committee in October 2017;
- a shortlist of candidates was then selected based on both their desire to be considered for the role and on the Committee's assessment of their career background and experience;
- after an initial interview with the Chairman, three preferred candidates were selected by the Committee to go forward for formal interview;
- the interview process was led by the Chairman and Senior Independent Director; the candidates were also interviewed by the other non-Executive Directors and by the outgoing CEO and the Group Finance Director. Character references and psychometric tests were also undertaken on each candidate;
- a preferred candidate recommendation was made by the Committee in December 2017; and
- a sub-Committee met with the preferred candidate, to negotiate a remuneration package within the Directors' Remuneration Policy and the range recommended by the Remuneration Committee. The Committee subsequently made a recommendation to the Board to appoint Richard Ingram, which the Board approved. Richard Ingram joined the Board as Chief Executive Officer designate on 23 April 2018 and became Chief Executive Officer on 8 May 2018.

Richard Ingram stepped down as CEO and Executive Director on 28 August 2018 and left the Company. John Nicholas was appointed by the Board as interim Executive Chairman and will remain in this role until a new CEO is appointed.

Following Richard Ingram's departure, the Nomination Committee commenced a new process to find a permanent replacement CEO. Korn Ferry, a search consultancy, was appointed to assist with the process. Korn Ferry does not provide any other services to and has no other connection with the Company. The Committee will follow a similar appointment process as adopted in 2017, amended to reflect shareholder feedback and Committee review. As at the date of this report, the process remains ongoing and the Board will make an announcement when an appointment decision has been finalised.

## SUCCESSION PLANNING

The Committee formally reviews succession planning for the Executive Board at least once each year, taking into account the challenges and opportunities facing the Group and the background skills and expertise that will be required by the Board in the future. As part of this exercise, development plans are also discussed and agreed to identify potential successors considered for appointment to the Board from within senior management within the Group.

In January each year, the Committee also reviews succession planning risks and opportunities in relation to the Company's senior executives, which comprise a cadre of ca. 100 senior managers across the Group's businesses.

The Committee regularly reviews the succession planning for non-Executive Directors. The Committee is committed to a programme of reviewing and refreshing the non-Executive Directors on the Board to ensure there is sufficient balance between the introduction of fresh perspectives and maintaining continuity and stability. The Committee intends to pursue a phased transition of non-Executives in order to avoid wholesale changes to the make-up of the Board over the next few years.

As part of the review of the composition of the Board and the succession planning process set out above, both the Board and the Committee recognise the importance of pursuing opportunities for both gender and ethnic diversity throughout the Group. The Board's commitment to gender and ethnic diversity is set out on page 40.

## COMMITTEE EVALUATION

As explained on page 41, an external evaluation of the performance of the Committee and its members was undertaken during the year. The Chairman and Company Secretary were asked to prepare an action list and timetable for the Committee to implement key recommendations arising from this exercise, although the evaluation confirmed that the Committee was operating effectively.

## KEY DUTIES AND FOCUS IN 2018

The Committee reviews the composition of the Board and principal Committees, considering skills, knowledge, experience and diversity requirements before making appropriate recommendations to the Board as to any changes. It also manages succession planning for Directors and other Senior Executives and is responsible for reviewing the Group's senior leadership needs.

The Committee's role and responsibilities are set out in its Terms of Reference, which are reviewed every two years and approved by the Board. The Terms of Reference are available at [www.diplomapl.com/governance/constitutional-documents](http://www.diplomapl.com/governance/constitutional-documents).

The Committee's key focus areas during the year have been the CEO succession, leadership development and executive succession planning.

# REMUNERATION COMMITTEE REPORT

**OUR REMUNERATION POLICY  
ALIGNS WITH BEST PRACTICE AND  
PROVIDES A STRONG BASIS FOR LINKING  
DIPLOMA'S STRATEGY AND PERFORMANCE  
TO EXECUTIVE REMUNERATION**

Andy Smith, Chairman of the Remuneration Committee

STRATEGIC REPORT

GOVERNANCE

FINANCIAL STATEMENTS

Members of Committee	Attendance
Andy Smith (Chairman)	6/6
Anne Thorburn	6/6
John Nicholas (until 31 August 2018)	6/6
Charles Packshaw	6/6

## DEAR SHAREHOLDER

This is the first year of the new Remuneration Policy ("the Policy") that shareholders adopted at this year's AGM. I am pleased to report that the Policy has worked well and continues to align with latest best practice. Company performance has once again been very strong this year as management continue to successfully execute the Company's strategy.

The Committee set the trigger for maximum payment under the annual performance bonus plan at 10% adjusted operating profit growth on a constant currency basis. In the year, the Company delivered an impressive 11.7% on this measure. Accordingly, Executives were awarded maximum payment.

Long term performance has been impressive too. The long term incentive plan targets relate to annual growth in earnings per share ("EPS") and relative total shareholder returns ("TSR") compared with the FTSE250 (excluding investment trusts) over a three-year period. To achieve the maximum award, Executives needed to achieve a minimum 14% EPS growth and 14.4% TSR in each of the three years of the performance period. They achieved 13.9% and 25.9% respectively, which translated into a payment of 99.6% of the maximum award under the long term incentive plan. The Committee is content that there is a strong alignment between performance delivery and these awards.

This year's Annual Report on Remuneration is set out in full on pages 51 to 63 of the Annual Report & Accounts and reflects the Remuneration Policy approved by shareholders in 2018. There were three matters, both relating to CEO remuneration that required careful judgement of the Committee in its application of the Policy.

The Company said farewell this year to Bruce Thompson, former CEO, after 22 years. The Committee had no hesitation in acknowledging Bruce's long and outstanding service for the Company during which he shaped Diploma into the Company it is today and consistently delivered excellent value for shareholders. Full details are available on page 56 but, in summary, the Committee treated him as a good leaver and approved early-vesting of his long term incentives, appropriately performance-tested and pro-rated for time served.

The Committee developed and approved a competitive package for Richard Ingram to attract him to join the Company as CEO. In line with the Policy, this took account of the remuneration package he had received in his former employment. When he stepped down from the Company, the Committee carefully and thoroughly considered its obligations to shareholders with specific reference to the Policy and the legal and contractual commitments made to Richard Ingram. The Committee approved payments to him under a settlement agreement that were in line with the Policy and were no more than was fair and reasonable in the circumstances. Details are set out on pages 56 and 57.

The Committee also considered the exceptional circumstances that will prevail whilst the Company works through the recruitment, appointment and on-boarding of a new CEO and in particular, the significant additional load and responsibility that will fall to the Group Finance Director. The Committee believes that it is in shareholders' interests to grant an LTIP award in 2019 of 225% of salary as allowed by Policy in such exceptional circumstances.

Base salaries for the new financial year (that is, from 1 October 2018) will increase by 3.0% (2017: 3.0%) for Executive Directors and by 4.5% across the senior management cadre. This reflects general pay inflation in the geographies the Company operates in.

Executive remuneration continues to attract attention, analysis and debate. The Committee will continue to note emerging views and trends and take an active role in reviewing the overall remuneration at senior levels in the organisation to ensure that they remain consistent with the actual performance delivered and are effective in attracting and retaining talent for the Group.

The Report of the Remuneration Committee was approved by the Board on 19 November 2018.

I look forward to meeting shareholders at this year's AGM on 16 January 2019 and will be pleased to answer any questions or concerns they have on the Company's remuneration policies.

Andy Smith  
19 November 2018

# REMUNERATION COMMITTEE REPORT CONTINUED

## REMUNERATION COMMITTEE

The Remuneration Committee ("the Committee") is chaired by Andy Smith and comprises independent non-Executive Directors. John Nicholas stepped down from the Committee on 31 August 2018, following his appointment as interim Executive Chairman.

The interim Executive Chairman/Chief Executive Officer attends meetings at the invitation of the Committee to provide advice to the Committee to help it make informed decisions. The Group Company Secretary attends meetings as Secretary to the Committee.

## THE REMUNERATION COMMITTEE REPORT

The Report has again been presented this year in two sections. The first section repeats the key elements of the Director's Remuneration Policy, which was approved by shareholders at the AGM on 17 January 2018. This Policy, which was set out in the 2017 Annual Report, will continue for a period of three years until 16 January 2021, unless replaced or amended by a new Policy.

The second section of this Report sets out the annual remuneration paid to the Directors in the year ended 30 September 2018 in accordance with the Policy approved on 17 January 2018. This section of the Report will continue to be subject to an advisory vote by shareholders at the AGM.

## REMUNERATION PRINCIPLES AND STRUCTURE

The Committee has adopted remuneration principles which are designed to ensure that senior executive remuneration:

- is aligned to the business strategy and promotes the long term success of the Company;
- supports the creation of sustainable long term shareholder value;
- provides an appropriate balance between remuneration elements and includes performance-related elements that are transparent, stretching and rigorously applied;
- provides an appropriate balance between immediate and deferred remuneration; and
- encourages a high-performance culture by ensuring performance-related remuneration constitutes a substantial proportion of the remuneration package and by linking maximum payout opportunity to outstanding results.

The Policy Table set out on the next page summarises the components of reward for the Executive Directors of Diploma PLC that will govern the Company's intentions as regards future payments. More detailed descriptions of the incentive plans are given in the following sections.

There have been no changes made to this Policy since it was approved by shareholders at the AGM on 17 January 2018.

## KEY DUTIES AND FOCUS IN 2018

The Remuneration Committee agrees, on behalf of the Board, all aspects of the remuneration of the Executive Directors and the Executive Committee, and agrees the strategy, direction and policy for the remuneration of the senior executives who have a significant influence over the Group's ability to meet its strategic objectives.

The Committee's role and responsibilities are set out in its Terms of Reference, which are reviewed annually and approved by the Board. The Terms of Reference are available on Diploma PLC's website at [www.diplomaplc.com/governance/constitutional-documents](http://www.diplomaplc.com/governance/constitutional-documents).

The Committee's key responsibilities and focus during the year have been:

- Reviewed Executive Directors' salaries, pensions and benefits.
- Approved Annual Performance Bonus targets and the subsequent bonus awards for 2018.
- Approved new PSP awards to Executive Directors and confirmed the performance conditions for such awards.
- Approved Recruitment Award Agreement and Long Term Incentive Award for new CEO.
- Approved retirement arrangements for Bruce Thompson.
- Approved remuneration aspects relating to the termination of Richard Ingram's employment.
- Accepted resignation of John Nicholas from the Remuneration Committee and approved interim Executive Chairman fees.
- Confirmed the vesting percentages for the PSP awards made in December 2015 which crystallised in 2018.
- Approved the exercise of nil cost options.
- Approved the 2018 Remuneration Committee Report.
- Reviewed the AGM 2018 votes on the 2017 Remuneration Committee Report and the 2018 Policy.
- Reviewed remuneration of senior management in the operating businesses.
- Approved updates to the rules of the Long Term Incentive Plan, required by the adoption of the new Policy and for new legislation (i.e. General Data Protection Regulation).
- Maintained watching brief on external reports on Directors' remuneration.
- Approved Remuneration Committee work programme for 2018.

## DIRECTORS' REMUNERATION POLICY

### THE REMUNERATION POLICY TABLE

The Remuneration Policy Table set out below summarises the components of reward for the Executive Directors of Diploma PLC that will govern the Company's intentions as regards future payments of remuneration until 16 January 2021, unless replaced or amended by a new Policy.

Executive Directors				
Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
<b>Base salary</b>	To attract and retain people of the calibre and experience needed to develop and execute the Company's strategy.	Salaries are reviewed annually, with changes normally effective from 1 October.	There is no maximum limit set. Salaries are targeted at a mid-market range for equivalent roles in similar companies.  Salary increases will generally be no higher than those awarded to other employees, although the Committee retains discretion to award larger increases if it considers it appropriate.	Salary levels and increases are determined based on a number of factors, including individual and business performance, level of experience, scope of responsibility, salary increases both for UK employees and for the senior management cadre more generally and the competitiveness of total remuneration against companies of a similar size and complexity.
<b>Pensions</b>	Designed to be competitive within the market to reward sustained contribution by Executive Directors.	Pension contributions up to 20% of base salary, which are either paid into personal pension savings schemes or paid as a separate cash allowance.	No maximum limit set.	No performance metric.
<b>Benefits</b>	To provide a competitive package of benefits.	Includes various cash/non-cash benefits such as: payment in lieu of a company car, life assurance, income protection, annual leave, medical insurance.	No maximum limit is prescribed, but the Committee monitors annually the overall cost of the benefit provision.	No performance metric.
<b>Annual Performance Bonus Plan</b>	To incentivise and reward Executive Directors on the achievement of the annual budget and other business priorities for the financial year.	Provides an opportunity for additional reward based on annual performance against targets set and assessed by the Committee.  Where shareholding guidelines have not been met, half of any annual bonus awarded (net of tax) will be deferred in shares for up to three years, but will remain eligible for dividends. The remaining bonus shall be paid in cash following the relevant year end.  Malus and clawback provisions apply.	Maximum of 125% of base salary for the Chief Executive Officer and 100% for other Executive Directors.  Performance below threshold results in zero payment. On-target bonus is 50% of maximum bonus and threshold performance is 5% of base salary.	Performance metrics are selected annually based on the current business objectives. The majority of the bonus will be linked to financial performance.  For FY2018, bonuses are based on adjusted operating profit (as defined in note 2 to the consolidated financial statements) on a constant currency basis.  Discretion to reduce awards if satisfactory threshold levels are not achieved for adjusted operating margin, free cash flow or ROATCE.  Different performance measures, including personal objectives, may be used for future cycles to take into account changes in the business strategy. Personal objectives, if used, will account for no more than 20% of the bonus.

## REMUNERATION COMMITTEE REPORT CONTINUED

### DIRECTORS' REMUNERATION POLICY CONTINUED

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
<b>Long Term Incentive Plan – PSP Awards</b>	Align Executive Directors to the Company's long term strategy and incentivise Executive Directors to achieve superior returns and long term value growth for shareholders.	<p>Performance assessed over rolling three-year performance periods.</p> <p>Awards are discretionary and do not vest until the date on which the performance conditions are determined. If employment ceases during a three-year performance period, other than in the case of a "good leaver", awards will normally lapse.</p> <p>For awards granted after the adoption of the new Policy on 17 January 2018, Executive Directors will be required to retain shares vesting under the LTIP (net of tax) until the fifth anniversary of grant.</p> <p>Awards may include dividend equivalents, which are cash bonuses or shares in lieu of dividends forgone on vested shares, from the time of award up to the time of vesting.</p> <p>Malus and clawback provisions apply.</p>	<p>The maximum opportunity as a percentage of salary is 175% for each award made to the Executive Directors under the 2011 Performance Share Plan ("PSP"). The Committee has discretion to increase awards under the PSP to 250% of salary in exceptional circumstances.</p> <p>No more than 25% of the award will be payable at threshold performance.</p>	<p>Awards will be granted subject to a combination of financial measures (including, for example, adjusted EPS, ROATCE and TSR), tested over a period of at least three years.</p> <p>The Committee may change the weighting of the performance measures or introduce new performance measures for future awards, so that they are aligned with the Company's strategic objectives.</p>
<b>Chairman and non-Executive Directors</b>				
Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
<b>Chairman and non-Executive Directors' fees</b>	To attract and retain a Chairman and independent non-Executive Directors of the required calibre and experience.	<p>Paid quarterly in arrears and reviewed each year.</p> <p>Any reasonable business related expenses (including tax thereon) can be reimbursed.</p>	The Chairman's and non-Executive Directors' fees are determined by reference to the time commitment and relevant benchmark market data.	Annual Board evaluation.

## EXECUTIVE DIRECTORS

### Base salary

In determining the annual base salary increases that apply from 1 October, the Committee considers comparative salaries in companies of a similar size and complexity and the range of remuneration increases applying across the Group.

The Committee also takes into account the salary increases applying across the senior management cadre. This comparator group comprises ca. 100 senior managers across the Group's businesses. This senior management cadre has been chosen as a representative group, as it provides a meaningful comparison considering the global and diverse nature of the Group's business.

### Annual performance bonus

The Diploma PLC Annual Performance Bonus Plan is substantially a cash based scheme designed to reward Executive Directors for meeting stretching annual performance targets.

Under the new Policy approved by shareholders at the AGM on 17 January 2018, the previous financial performance target of "adjusted EPS" was replaced by "Group adjusted operating profit" that is calculated on a basis that excludes the impact of currency on the translation of Group adjusted operating profit. The replacement performance target applies to the financial year ended 30 September 2018 and thereafter.

At the start of the financial year (1 October), the Board sets a financial performance target principally focused on achievement of a target Group adjusted operating profit. Adjusted operating profit is calculated on a constant currency basis. The level of bonus payable for achieving the minimum target is 5% of base salary. No bonus is payable if performance does not meet the minimum target.

The definition of adjusted operating profit is consistent with the Group's financial statements (see note 2). However, the Committee has discretion to modify the definition in the event of changes in accounting policy and/or material operational, market, exchange rate or environmental factors in order to more appropriately reflect management performance. The Committee has discretion to reduce awards if minimum thresholds are not achieved for adjusted operating margins, free cash flow and return on adjusted trading capital employed ("ROATCE"). Where used, the rationale for the exercise of this discretion will be disclosed in the next Remuneration Committee Report.

Different performance measures may be used for future cycles of the Annual Performance Bonus Plan to those set out in the Policy Table to take into account changes in the business strategy.

While retaining flexibility under the Policy, in relation to the setting of individual objectives, the bonus payable for the financial year ending 30 September 2018 and thereafter is based solely on adjusted operating profit on a constant currency basis.

At the end of the financial year, the Committee meets to assess the performance of each Executive Director against the bonus targets. Bonuses are normally paid in cash in December.

The Policy requires that 50% of any bonus awarded for the financial year ending 30 September 2018 or thereafter, is deferred on a net of tax basis into shares until minimum shareholding guideline levels, set at 200% of base salary for Executive Directors under the Policy, have been met.

### Long term incentive award

The Company operates a long term incentive award plan for Executive Directors, the Diploma PLC 2011 Performance Share Plan ("PSP"). The PSP is designed to promote the long term success of the Company, while also aligning the Directors' interests with those of Diploma PLC shareholders.

The PSP provides for a grant of conditional awards of a specified number of ordinary shares in the Company, or an option to acquire a specified number of shares at an exercise price determined by the Committee (which may be nil or a nominal amount). No payment is required for the grant of an award.

Awards, which are normally granted annually, must generally be made within 42 days after the announcement of the Company's annual results. When making the decision on the level of award, the Committee takes into consideration a number of factors, including the face value of the award and plan dilution limits.

The face value of an award is equal to the number of shares, or shares under option, multiplied by the relevant share price. The relevant share price will be the mid-market closing share price on the dealing day before the award. A face value limit of 175% of base salary applies to each PSP award to Executive Directors, although the Committee, at its discretion, may increase the face value of an award to a maximum of 250% in exceptional circumstances.

All awards will normally vest on the date on which the performance conditions are determined and confirmed by the Committee, following the end of the performance period. The vesting of awards is conditional on:

- continued employment;
- the Company's growth in adjusted EPS over a three-year performance period; and
- the Company's TSR performance over a three-year performance period.

The latter two performance conditions apply to each award so that the vesting of 50% of the award is based on growth in adjusted EPS and 50% of the award is based on the relative TSR performance. These measures align with our long term goal of value creation for shareholders through underlying financial growth and above-market shareholder returns.

Each performance condition is measured over a three-year period commencing on the first day of the financial year in which the award is made. There is no retesting of the performance metrics. At the minimum performance threshold, 25% of the PSP awards will vest.

The Committee will regularly monitor the continuing suitability of the performance conditions and may impose different performance conditions or targets for awards granted in subsequent years, to align with the Company's strategic objectives and having regard to prevailing market practice.

The Committee may decide, on or before the grant of a share incentive award, that on exercise of the award, the participants may receive, in addition to the shares in which they then become entitled, a dividend equivalent in respect of the dividends (excluding any tax credit) which would have been paid to the participant in respect of shares vesting between the date of the award and the time of vesting. These dividend equivalent payments may be made in cash or in an equivalent number of shares.

For awards granted after 17 January 2018, Executive Directors will be required to retain shares vesting under the LTIP (net of tax) until the fifth anniversary of grant ("the Holding Period"), to reflect developments in best practice and the Committee's continued focus on long term shareholder alignment. The Holding Period shall expire on the earliest of:

- the fifth anniversary of the date of grant of an award;
- the date of a change of control event;
- the death of the participant; or
- such other date as determined by the Committee in its discretion.

# REMUNERATION COMMITTEE REPORT CONTINUED

## DIRECTORS' REMUNERATION POLICY CONTINUED

### Service contracts

The Executive Directors' service contracts, including arrangements for early termination, are carefully considered by the Committee and are designed to recruit, retain and motivate Directors of the calibre required to manage the Company and successfully deliver its strategic objectives.

The Committee considers that a rolling contract with a notice period of one year is appropriate for existing and newly appointed Directors.

The Executive Directors' service contract, a copy of which is held at the Company's registered office, was updated in March 2014 to recognise developments in law and best practice relating to such contracts. This service contract, together with any service contract for new appointments, contains provisions for compensation in the event of early termination or change of control, equal to the value of salary and contractual benefits for the Director's notice period. The Company may make a payment in lieu of notice in the event of early termination and the Company may make any such payment in instalments with the Director being obliged in appropriate circumstances to mitigate loss (for example by gaining new employment).

The Committee considers that these provisions assist with recruitment and retention and that their inclusion is therefore in the best interests of shareholders.

Details of the service contracts of the Executive Directors who served during the year are set out below:

	Contract date	Unexpired term	Notice period	Compensation payable upon early termination
Bruce Thompson	20 Mar 2014	Retired, 8 May 2018	1 year	1 year
Richard Ingram	29 Jan 2018	Left, 28 Aug 2018	1 year	1 year
John Nicholas <sup>1</sup>	29 Aug 2018	Rolling	1 month	1 month
Nigel Lingwood	20 Mar 2014	Rolling	1 year	1 year

<sup>1</sup> John Nicholas was appointed interim Executive Chairman following the departure of Richard Ingram as Chief Executive Officer on 28 August 2018.

## OTHER REMUNERATION POLICIES

### Payment for loss of office

The Committee has considered the Company's policy on remuneration for Executive Directors leaving the Company and is committed to applying a consistent approach to ensure that the Company pays no more than is fair and reasonable in the circumstances.

The loss of office payment policy is in line with market practice and will depend on whether the departing Executive Director is, or is deemed to be treated as, a "good leaver" or a "bad leaver". In the case of a good leaver the Policy includes:

- Notice period of 12 months' base salary, pension and contractual benefits or payment in lieu of notice.
- Bonus payable for the period worked, subject to achievement of the relevant performance condition. Different performance measures (to the other Executive Directors) may be set for a departing Director as appropriate, to reflect any change in responsibility.
- Vesting of award shares under the Company's LTIP is not automatic and the Committee would retain discretion to allow partial vesting depending on the extent to which performance conditions had been met and the length of time the awards have been held. Time pro-rating may be disapplied if the Committee considers it appropriate, given the circumstances. For awards

granted prior to 17 January 2018, performance will be measured to the date of cessation of employment and, to the extent applicable, vest shortly thereafter. For awards granted after the adoption of the new Policy on 17 January 2018, performance will be measured to the end of the normal performance period and, to the extent applicable, vest on the normal vesting date, save in exceptional circumstances when the Committee may determine that early vesting should still apply.

- The Committee will provide for the leaver to be reimbursed for a reasonable level of legal fees in connection with a settlement agreement.

When calculating termination payments, the Committee will take into account a variety of factors, including individual and Company performance, the obligation for the Executive Director in appropriate circumstances to mitigate loss (for example, by gaining new employment) and the Executive Director's length of service.

The Committee reserves the right to make additional exit payments where such payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation) or by way of settlement or compromise of any claim arising in connection with the termination of a Director's office or employment.

### Change of control

Change of control provisions provide for compensation equal to the value of salary and contractual benefits for the notice period. In the event of a change in control, vesting of an award of shares under the Company's PSP depends on the extent to which performance conditions had been met at that time. Time pro-rating may be disapplied if the Committee considers it appropriate, given the circumstances of the change of control.

### Malus and clawback

Malus provisions apply to all awards made under the Company's long term incentive and annual bonus plans, which give the Committee the right to cancel or reduce unvested share awards (or in the case of the Annual Performance Bonus Plan, cash payments) in the event of material misstatement of the Company's financial results, miscalculation of a participant's entitlement or individual gross misconduct.

Clawback arrangements, which also apply to all awards made under the Company's long term incentive and annual bonus plans, permit the Committee to recover amounts paid to Executive Directors in specified circumstances to safeguard shareholders' interests.

### Remuneration for new appointments

The Committee has determined that new Executive Directors will receive a compensation package in accordance with the terms of the Group's approved Policy in force at the time of appointment.

The Committee has agreed the following principles that will apply when arranging a remuneration package to recruit new Executive Directors:

- The remuneration structure will be kept simple where practicable, hence the use of base salary, benefits, pension (or cash allowance in lieu), annual performance bonus and long term incentives.
- The emphasis on linking pay with performance shall continue; hence the use of variable pay in the form of an annual performance bonus and a long term incentive award, which will continue to be a significant component of the Executive Directors' total remuneration package.
- Initial base salary will take into account the experience and calibre of the individual and their existing remuneration package. Where it is appropriate to offer a lower salary initially, a series of increases to the desired salary positioning may be given over subsequent years subject to individual performance.



- The structure of variable pay will be in accordance with Diploma's approved Policy, set out above, with an exceptional maximum aggregate variable pay opportunity of 375% of salary. Different performance measures may be set in the first year for the annual bonus, taking account of the responsibilities of the individual and the point in the financial year that the executive joined the Company.
- Benefits will generally be provided in accordance with the approved Policy, with relocation expenses and an expatriate allowance paid if appropriate.
- In the case of an external recruitment, the Committee may also offer additional cash and/or share-based elements when it considers these to be in the best interests of Diploma and shareholders, to replace variable remuneration awards or arrangements that an individual has foregone in order to join the Group. This includes the use of awards made under section 9.4.2 of the UK Listing Rules. Any such payments would take account of the details of the remuneration foregone including the nature, vesting dates and any performance requirements attached to that remuneration and any payments would not exceed the expected value being forfeited.
- In the case of an internal appointment, any outstanding variable pay awarded in relation to the previous role will be allowed to pay out according to the terms of grant.
- For all new Executive Director appointments, the mandated shareholding guidelines, deferral of annual performance bonus and the Holding Period for LTIP awards will apply in accordance with the Policy and the relevant Plan rules.
- Fees for a new Chairman or non-Executive Director will be set in line with the approved Policy.

#### Committee discretion

The Committee operates the Annual Performance Bonus Plan and the LTIP in accordance with the relevant plan rules and where appropriate, the Listing Rules and HMRC legislation. As a matter of course, the Committee will normally seek to avoid the use of discretion. However in order to ensure that outcomes are always in the interests of shareholders, the Committee retains discretion over a number of areas relating to the operation and administration of the plans. These include, the timing of awards and of the setting of performance criteria each year, dealing with leavers, discretion to waive or shorten the Holding Period for shares acquired under the LTIP, the discretion to retrospectively amend performance targets in exceptional circumstances and in respect of share awards, to adjust the number of shares subject to an award in the event of a variation in the share capital of the Company. The Committee will exercise its powers in accordance with the terms of the relevant plan rules. The Committee also has discretions to set components of remuneration within a range from time to time as set out in the maximum opportunity sections of the Policy Table.

#### Dilution

In any ten-year period, the number of shares which are or may be issued under option or other share awards under any discretionary share plan established by the Company may not exceed 5% of the issued ordinary share capital of the Company from time to time. In any ten-year period, the aggregate number of shares that are or may be issued under option, or other share awards under all share plans established by the Company, may not exceed 10% of the issued ordinary share capital of the Company, from time to time.

#### Consultation with shareholders and employees

The Committee will consult with its major shareholders in advance of any significant changes to the approved Policy or exercise of discretion, as appropriate, to explain their approach and rationale fully and to understand shareholders' views. Additionally, the Committee considers shareholder feedback received in relation to each AGM alongside any views expressed during the year. The Committee also reviews the executive remuneration framework in the context of published Investor Guidelines.

The Committee does not consult directly with employees when formulating the Policy for Executive Directors.

#### Policy in respect of external board appointments for Executive Directors

The Committee recognises that external non-Executive directorships may be beneficial for both the Company and the Executive Director. At the discretion of the Board, Executive Directors are permitted to retain fees received in respect of any such non-Executive directorship.

#### Shareholding guidelines

The Committee has adopted guidelines for Executive Directors, to encourage substantial long term share ownership. These specify that, over a period of five years from the date of appointment, each Executive Director should build up and then retain a holding of shares with a value equivalent to 200% of base salary. The guidelines also require that, in relation to long term incentive awards, vested shares (net of tax) must be retained by the individual until the required shareholding level is reached.

#### CHAIRMAN AND NON-EXECUTIVE DIRECTORS

##### Recruitment and term

The Board aims to recruit non-Executive Directors of a high calibre, with broad and diverse commercial, international or other relevant experience. Non-Executive Directors are appointed by the Board on the recommendation of the Nomination Committee. Appointments of the non-Executive Directors are for an initial term of three years, subject to election by shareholders at the first AGM following their appointment and subject to annual re-election thereafter. The terms of engagement are set out in letters of appointment that can be terminated by either party serving three months' notice.

##### Chairman

John Nicholas was appointed Chairman on 21 January 2015, having previously been the Senior Independent Director. His appointment is subject to annual re-election by shareholders at the AGM. John Nicholas was appointed interim Executive Chairman on 28 August 2018.

Chairman and non-Executive Directors' letters of appointment:

	Date of original appointment	Date of re-election	Expiry of term
John Nicholas	1 Jun 13	17 Jan 18	20 Jan 21
Charles Packshaw	1 Jun 13	17 Jan 18	1 Jun 19
Andy Smith	9 Feb 15	17 Jan 18	9 Feb 21
Anne Thorburn	7 Sep 15	17 Jan 18	7 Sep 21

##### Fees

The non-Executive Directors are paid a competitive basic annual fee, which is approved by the Board on the recommendation of the Chairman and the Executive Directors. The Chairman's fee is approved by the Committee, excluding the Chairman. Additional fees may also be payable for chairing a Committee of the Board or for acting as Senior Independent Director. The fees are reviewed each year and take account of the fees paid in other companies of a similar size and complexity, the non-Executive Directors responsibilities and the required time commitment.

If there is a temporary yet material increase in the time commitments for non-Executive Directors, the Board may pay extra fees on a pro-rata basis to recognise the additional workload. In 2018, the Board approved an additional fee of £144,600 per annum to be payable to the Chairman, while he serves as interim Executive Chairman.

The non-Executive Directors are not eligible to participate in any of the Company's share plans, incentive plans or pension schemes and there is no provision for payment in the event of early termination.

# REMUNERATION COMMITTEE REPORT CONTINUED

## ANNUAL REPORT ON REMUNERATION

The following section of this Report provides details of the implementation of the existing Remuneration Policy for the Executive Directors for the years ended 30 September 2018 and 2017. All of the information set out in this section of the Report has been audited, unless indicated otherwise.

### EXECUTIVE DIRECTORS

#### Total remuneration in 2018 and 2017

	John Nicholas <sup>1</sup>	Richard Ingram <sup>2</sup>	Bruce Thompson <sup>3</sup>		Nigel Lingwood	
	2018 £000	2018 £000	2018 £000	2017 £000	2018 £000	2017 £000
Fees/Salary	14	191	303	486	323	314
Benefits	-	9	15	24	18	18
Pension	-	35	61	97	65	63
Annual performance bonus	-	-	625	607	323	310
Short term remuneration (cash)	14	235	1,004	1,214	729	705
Long term incentive plans – dividend equivalent (cash)	-	-	102	43	46	28
Long term incentive plans – performance element (non-cash)	-	-	1,677	714	534	461
Long term incentive plans – share appreciation element (non-cash)	-	-	1,059	287	501	186
Total long term share price based remuneration (non-cash)	-	-	2,736	1,001	1,035	647
<b>Total</b>	<b>14</b>	<b>235</b>	<b>3,842</b>	<b>2,258</b>	<b>1,810</b>	<b>1,380</b>

<sup>1</sup> John Nicholas was appointed interim Executive Chairman on 28 August 2018. The fees above relate to his Executive service from 28 August to 30 September 2018; as interim Executive Chairman, John Nicholas is not entitled to benefits, pension, annual bonus or an LTIP. John Nicholas's fees for his role as non-Executive Chairman are set out on page 63.

<sup>2</sup> Richard Ingram's salary, benefits and pension are for the period from appointment as Chief Executive Officer (designate) on 23 April 2018 to 28 August 2018, when he stood down as Chief Executive Officer and Executive Director and left the Company. Further details regarding his remuneration are set out below.

<sup>3</sup> Bruce Thompson's salary, benefits and pension are for the period from 1 October 2017 to 8 May 2018, while he served as Chief Executive Officer and Executive Director of the Company. The table above includes his annual performance bonus and the full value of all long term incentive awards that vested at 30 September 2018. Bruce Thompson's salary for the period from 9 May 2018 to 30 September 2018 was £197,000.

The aggregate short term remuneration paid to Executive Directors in the year ended 30 September 2018 was £2.0m (2017: £1.9m).

### RETIREMENT OF BRUCE THOMPSON

Bruce Thompson retired as Chief Executive Officer and as an Executive Director of the Company on 8 May 2018; he retired as an employee of the Company on 30 September 2018. Bruce Thompson was treated as a "good leaver" as he had played the leading role in developing and implementing the successful growth strategy of the Group over many years. Bruce Thompson's long term incentive awards vested to the extent to which the applicable performance conditions were met. These awards were pro-rated for time served, (that is, two out of three years and one out of three years for awards that would, but for his retirement, have vested at 30 September 2019 and 30 September 2020, respectively). The vesting of these awards was based on the testing of the performance criteria for the year ended 30 September 2018.

### REMUNERATION ARRANGEMENTS FOR RICHARD INGRAM

#### Appointment

On 23 April 2018, Richard Ingram joined the Board as Chief Executive Officer (designate). Bruce Thompson retired from the Board and handed over his Chief Executive Officer responsibilities to Richard Ingram at the close of the Board meeting on 8 May 2018.

Richard Ingram was to receive an annual salary of £535,000 and a pension allowance of 15% of base salary. Richard Ingram was also eligible to participate in both the Annual Bonus Plan (up to a maximum of 125% of base salary) and in the LTIP up to 175% of base salary. All of these remuneration arrangements are consistent with the terms of the Directors' Remuneration Policy approved by shareholders on 17 January 2018.

The Board also agreed in accordance with the Remuneration Policy to compensate Richard Ingram on his appointment as Chief Executive Officer to replace the balance of his existing incentives from his previous employment. To replace incentives relating to the year ended 30 September 2018, Richard Ingram was eligible for a performance bonus of £1.0 million before tax, of which up to 40% was payable in cash and the balance in the form of a nil cost option over Company shares. To replace incentives relating to the years ending September 2019 and September 2020, Richard Ingram was also eligible to receive a long term incentive award (nil cost option) over shares in the Company, on terms similar to the Company's LTIP, representing 116.7% and 175% of his base salary with vesting dependent upon performance conditions.

#### Departure and payment for loss of office

Ingram stepped down from his role as Chief Executive Officer and Executive Director and left the Company on 28 August 2018. The financial terms below were agreed with Richard Ingram in a settlement agreement dated 8 November 2018. These payments are in accordance with the shareholder approved Remuneration Policy and the Company is honouring its contractual commitments.

The following arrangements will apply in respect of Richard Ingram's notice period:

- Richard Ingram will receive the sum of £507,200 as a payment in lieu of his unworked contractual notice period. A 20% deduction was applied to the full 12 month notice entitlement (£634,137) by way of mitigation.

Other terms agreed with Richard Ingram in November 2018, which were the subject of careful consideration by the Remuneration Committee were as follows:

- an additional exit payment of £360,000 by way of settlement of potential claims by Richard Ingram for loss of bonus and incentive opportunities; and
- a contribution of £20,000 (plus VAT) towards Richard Ingram's legal fees incurred in connection with the above arrangement.

No other payments were made to Richard Ingram under either the annual performance bonus plan, the long term incentive award or the recruitment award, all of which lapsed as at 30 September 2018.

#### EXECUTIVE DIRECTORS' OTHER ROLES

John Nicholas is non-Executive Chairman of Porvair plc and received fees of £8,804 for the period from 28 August 2018 to 30 September 2018. Bruce Thompson was appointed non-Executive Director of DiscoverIE Group plc on 26 February 2018 and received fees of £8,914 during the period from 26 February 2018 to 8 May 2018.

#### Base salary

The average base salary increase for Executive Directors which applied from 1 October 2017 was 3.0%, compared with 6.5% for the Group's senior management cadre. On 13 November 2018, the Committee approved an increase of 3.0% in base salary for the interim Executive Chairman and the Group Finance Director that will apply in respect of the year commencing 1 October 2018 which compares with 4.5% for the Group's senior management cadre.

#### Benefits

	2018				2017			
	Cash allowance in lieu of a car £000	Life assurance and income protection £000	Medical insurance £000	Total benefit £000	Cash allowance in lieu of a car £000	Life assurance and income protection £000	Medical insurance £000	Total benefit £000
John Nicholas <sup>1</sup>	-	-	-	-	-	-	-	-
Richard Ingram <sup>2</sup>	5	3	1	9	-	-	-	-
Bruce Thompson <sup>3</sup>	9	4	2	15	13	7	4	24
Nigel Lingwood	11	6	1	18	11	6	1	18

<sup>1</sup> John Nicholas is not entitled to benefits in his role as interim Executive Chairman.

<sup>2</sup> Richard Ingram's benefits are for the period from 23 April 2018 to 28 August 2018.

<sup>3</sup> Bruce Thompson's benefits are for the period from 1 October 2017 to 8 May 2018; his benefits for the period from 9 May 2018 to 30 September 2018 were £9,000.

#### Pension

The Executive Directors receive pension contributions from the Company, which they may pay into personal savings vehicles or may take as a separate cash allowance, subject to income tax.

Pension contributions were applied as follows:

Contribution contributions were applied as follows:

	2018				2017			
	Contribution rate % of base salary	Paid as cash allowance £000	Paid as pension contribution £000	Total cash paid £000	Paid as cash allowance £000	Paid as pension contribution £000	Total cash paid £000	
John Nicholas <sup>1</sup>	-	-	-	-	-	-	-	
Richard Ingram <sup>2</sup>	15	35	-	35	-	-	-	
Bruce Thompson <sup>3</sup>	20	61	-	61	97	-	97	
Nigel Lingwood	20	65	-	65	63	-	63	

<sup>1</sup> John Nicholas is not entitled to a pension contribution in his role as interim Executive Chairman.

<sup>2</sup> Richard Ingram's pension contributions are for the period from 23 April 2018 to 28 August 2018.

<sup>3</sup> Bruce Thompson's pension contributions are for the period from 1 October 2017 to 8 May 2018; his pension contributions for the period from 9 May 2018 to 30 September 2018 were £39,000.

# REMUNERATION COMMITTEE REPORT CONTINUED

## ANNUAL REPORT ON REMUNERATION CONTINUED

### Annual performance bonus

The following table summarises the performance assessment by the Committee in respect of 2018 with regard to the Group financial objectives:

Performance measure	Performance in 2018	Overall assessment against targets
Adjusted Operating Profit (on a constant currency basis)	The minimum performance target was equal to the 2017 adjusted Operating Profit (as defined in note 2 to the consolidated financial statements) on a constant currency basis. The on-target performance was equal to the FY2018 budget (4% growth on 2017). The maximum target was at least 10% growth above 2017 adjusted Operating Profit. Adjusted Operating Profit (on a constant currency basis) grew by 11.7%. Minimum thresholds were exceeded for adjusted operating margins, free cash flow and ROATCE.	100% of the maximum award

Based on the performance set out above, the resulting bonus for each Executive Director relating to 2018 is as follows:

	2018 actual bonus – as a percentage of 2018 base salary					2018 bonus delivered as cash £000
	Minimum	On-target	Maximum	Financial objectives	Total bonus	
John Nicholas <sup>1</sup>	–	–	–	–	–	–
Richard Ingram <sup>2</sup>	5%	63%	125%	125.0%	–	–
Bruce Thompson <sup>3</sup>	5%	63%	125%	125.0%	125.0%	625
Nigel Lingwood	5%	50%	100%	100.0%	100.0%	323

<sup>1</sup> John Nicholas is not entitled to a bonus in his role as interim Executive Chairman.

<sup>2</sup> Richard Ingram was not awarded a bonus for the year ended 30 September 2018.

<sup>3</sup> Bruce Thompson's bonus is for the period from 1 October 2017 to 30 September 2018.

The Annual Performance Bonus for the financial year beginning 1 October 2018 will be based solely on adjusted operating profit, measured on a constant currency basis. The financial performance targets set for the Annual Performance Bonus will be disclosed in next year's Annual Report & Accounts.

### Long term incentive awards

#### Performance conditions

Set out below is a summary of the performance conditions that apply to the PSP awards that vest in 2018 and the outstanding PSP awards, including those granted in December 2016 and December 2017. PSP awards since 1 October 2014 have been granted at 175% of base salary. The performance conditions applying to these awards made under the PSP are set out below. In determining the 2019 long term incentive award for the Executive Director, the Committee considered the exceptional circumstances that will prevail whilst the Company works through the recruitment, appointment and on-boarding of a new CEO. During this period, a significant additional load and responsibility will fall to the Group Finance Director, Nigel Lingwood. The Committee believes that it is in shareholders' interests in these exceptional circumstances to provide him with additional incentivisation. Accordingly and as allowed under the Policy, a grant of 225% of salary for the 2019 long term incentive was approved.

The performance condition for the first half of the PSP awards is that the average annual compound growth in the Company's adjusted EPS, over the three consecutive financial years following the financial year immediately prior to the grant, must exceed the specified absolute figures. The performance conditions are as follows:

Adjusted EPS growth (over three years)	% of awards vesting PSP
14% p.a.	100
5% p.a.	25
Below 5% p.a.	Nil

Where the Company's adjusted EPS performance is between these percentage bands, vesting of the award is on a straight-line basis. For the purposes of this condition, EPS is adjusted EPS as defined in note 2 to the consolidated financial statements and this definition remains consistent with the definition of adjusted EPS approved by the Committee in previous years.

The performance condition for the second half of the PSP awards compares the growth of the Company's TSR over a three-year period to that of the companies in the FTSE 250 Index (excluding Investment Trusts). The performance conditions are as follows:

	% of awards vesting PSP
Upper quartile	100
Median	25
Below median	Nil

Where the Company's TSR performance is between these percentage bands, vesting of the award is on a straight-line basis. The FTSE 250 Index was chosen because this is a recognised broad equity market index of which the Company is a member.

### Awards vesting in 2018

The PSP awards made to the Executive Directors on 17 December 2015, and the PSP awards made to Bruce Thompson on 22 December 2016 and 28 December 2017, were subject to operating performance conditions as set out in the table on page 58, independently assessed over a three-year period ended 30 September 2018 and for the 2016 and 2017 awards to Bruce Thompson only, over the two and one-year period ended 30 September 2018, respectively. The outcome of each award is shown in the table below:

Adjusted earnings per share:

	Base EPS	EPS at 30 Sep 2018	CAGR in EPS	Maximum target	Maximum award	Vested award
PSP (17 December 2015)	38.2p	<b>56.4p</b>	13.9%	14.0%	50%	49.6%
PSP (22 December 2016) <sup>1</sup>	41.9p	<b>56.4p</b>	16.0%	14.0%	50%	50.0%
PSP (28 December 2017) <sup>1</sup>	49.8p	<b>56.4p</b>	13.3%	14.0%	50%	47.1%

<sup>1</sup> Award vesting to Bruce Thompson only, following his retirement from the Board on 8 May 2018, on the basis explained on page 56.

TSR growth against FTSE 250 (excluding Investment Trusts):

	TSR at 30 Sep 2018	Median	Maximum target	Maximum award	Vested award
PSP (17 December 2015)	<b>25.9%</b>	5.3% p.a.	14.4% p.a.	50%	50.0%
PSP (22 December 2016) <sup>1</sup>	<b>28.5%</b>	12.1% p.a.	23.3% p.a.	50%	50.0%
PSP (28 December 2017) <sup>1</sup>	<b>28.4%</b>	3.75% p.a.	19.2% p.a.	50%	50.0%

<sup>1</sup> Award vesting to Bruce Thompson only, following his retirement from the Board on 8 May 2018, on the basis explained on page 56.

As a result of the above performance conditions, 99.6% of the shares awarded as nil cost options vested to each Director under the PSP award granted on 17 December 2015. In addition, 100% and 97.1% of the shares awarded as nil cost options under the PSP awards granted on 22 December 2016 and on 28 December 2017 respectively, vested to Bruce Thompson.

Set out below are the shares that vested to each Executive Director at 30 September 2018 in respect of these awards. The shares vesting to Bruce Thompson are stated after each of the awards have been time pro-rated to reflect his retirement as explained on page 56.

	Share price at date of grant pence	Share price at 30 Sep 2018 pence	Proportion of award vesting	Shares vested number	Performance element <sup>1</sup> £000	Share appreciation element <sup>2</sup> £000	Total £000
Bruce Thompson <sup>3</sup> – PSP	730p	1,416p	<b>99.6%</b>	<b>113,175</b>	827	776	<b>1,603</b>
– PSP (2016)	997.5p	1,416p	<b>100.0%</b>	<b>56,842</b>	567	238	<b>805</b>
– PSP (2017)	1,221p	1,416p	<b>97.1%</b>	<b>23,195</b>	283	45	<b>328</b>
Nigel Lingwood – PSP	730p	1,416p	<b>99.6%</b>	<b>73,063</b>	534	501	<b>1,035</b>
John Nicholas <sup>4</sup>	–	–	–	–	–	–	–

<sup>1</sup> The performance element represents the face value of awards that vested, having met the performance conditions set out above.

<sup>2</sup> The share appreciation element represents the additional value generated through appreciation of the share price from the date the awards were granted to the end of the three-year performance period on 30 September 2018, and additionally in the case of Bruce Thompson, the two and one-year periods ended 30 September 2018 respectively.

<sup>3</sup> The awards for Bruce Thompson have been pro-rated for two of three years for the 2016 PSP and pro-rated for one of three years for the 2017 PSP. These awards vested based on the testing of performance criteria for the period to 30 September 2018.

<sup>4</sup> John Nicholas is not eligible for any LTIPs.

### Dividend equivalent payments

Dividend equivalent payments of £117,516 (2017: £70,340) will be payable to Bruce Thompson and Nigel Lingwood in respect of the 2015 PSP awards which vested on 30 September 2018. These payments are included in this year's Annual Report on Remuneration. Dividend equivalent payments of £25,352 and £5,520 will be payable to Bruce Thompson in respect of awards which vested on 30 September 2018 relating to the 2016 PSP and 2017 PSP awards respectively.

### Long term incentive plan – awards granted in the year

Bruce Thompson and Nigel Lingwood received grants of PSP awards on 28 December 2017, in the form of nil-cost options as set out on page 60. These awards were based on a share price of 1,221p, being the mid-market price of an ordinary share in the Company at close of business on the day immediately preceding the award.

Under normal circumstances, the options will not become exercisable until the performance conditions are determined after the end of the three-year measurement period which begins on the first day of the financial year in which the award is made and provided the Director remains in employment. The level of vesting is dependent on the achievement of specified performance criteria at the end of the three-year measurement period.

The award granted on 28 December 2017 to Bruce Thompson vested to the extent to which the applicable performance conditions were met for the year ended 30 September 2018. The award was pro-rated for time served, that is on the basis of one out of three years completed.

The performance conditions for these awards are set out on page 58.

# REMUNERATION COMMITTEE REPORT CONTINUED

## ANNUAL REPORT ON REMUNERATION CONTINUED

### Outstanding share-based performance awards

Set out below is a summary of the share-based awards outstanding at 30 September 2018, including both share awards which have vested during the year (based on performance) and share awards which have been granted during the year. The awards set out below were granted based on a face value limit of 175% of base salary for each award. No awards will vest unless the performance conditions set out on page 58 are achieved.

### Diploma PLC 2011 Performance Share Plan

	Market price at date of award	Face value of the award at date of grant £000	End of performance period	Vesting date	Shares over which awards held at 1 Oct 2017	Shares over which awards granted during the year	Vested during the period	Lapsed during the period	Shares over which awards held at 30 Sep 2018
<b>Bruce Thompson<sup>1</sup></b>									
17 December 2015	730p	829	30 Sep 2018	30 Sep 2018	113,630	-	113,175	455	-
22 December 2016	997.5p	850	30 Sep 2019	30 Sep 2018	85,263	-	56,842	28,421	-
28 December 2017	1,221p	875	30 Sep 2020	30 Sep 2018	-	71,664	23,195	48,469	-
<b>Nigel Lingwood</b>									
17 December 2015	730p	535	30 Sep 2018	30 Sep 2018	73,356	-	73,063	293	-
22 December 2016	997.5p	549	30 Sep 2019	30 Sep 2019	55,035	-	-	-	55,035
28 December 2017	1,221p	565	30 Sep 2020	30 Sep 2020	-	46,294	-	-	46,294

<sup>1</sup> The awards for Bruce Thompson have been pro-rated for two of three years for the 2016 PSP award (85,263 shares awarded and pro-rated to 56,842 shares) and pro-rated for one of three years for the 2017 PSP award (71,664 shares awarded and pro-rated to 23,888 shares). These awards vested based on the testing of performance criteria for the period to 30 September 2018, as explained on page 56.

The PSP awards vest on the date on which the performance conditions are determined and confirmed by the Committee, following the end of the performance period.

The PSP awards are granted in the form of nil-cost options (there is a notional exercise price of £1 per award). To the extent that the awards vest, the options are then exercisable until the tenth anniversary of the award date; a good leaver must exercise his awards within 12 months of leaving the Company. Details of options exercised during the year and outstanding at 30 September 2018 are set out on page 62.

### Long Term Incentive Award (on recruitment)

	Market price at date of award	Face value of the award at date of grant £000	End of performance period	Vesting date	Shares over which awards held at 1 Oct 2017	Shares over which awards granted during the year	Vested during the period	Lapsed during the period	Shares over which awards held at 30 Sep 2018
<b>Richard Ingram<sup>1</sup></b>									
15 May 2018	1,233p	624	30 Sep 2019	30 Sep 2019	-	50,618	-	50,618	-
15 May 2018	1,233p	936	30 Sep 2020	30 Sep 2020	-	75,932	-	75,932	-

<sup>1</sup> Richard Ingram received a Long Term Incentive Award on 15 May 2018 in the form of nil-cost options. The award was made in accordance with Listing Rule 9.4.2R(2) and comprised 50,618 award shares with a two-year performance period to 30 September 2019 and 75,932 award shares with a three-year performance period to 30 September 2020. Both of these awards lapsed when Richard Ingram stood down as Chief Executive Officer and Executive Director on 28 August 2018.

### SERVICES FROM EXTERNAL ADVISORS (UNAUDITED)

Stephenson Harwood LLP provide legal advice to the Committee on remuneration matters and on the Directors' Remuneration Policy. Ashurst LLP provide legal advice on employment matters.

The Committee also received advice and assistance from Aon on market practice, governance trends and the application of Policy during the year. The Committee also engaged MEIS to provide certain data analyses to the Committee.

The Committee has considered and is satisfied that the advice received from the external advisors it has appointed is objective and independent. None of the advisors have any relationships with the Company.

Advisor	Appointed by	Services provided to the Committee	Other services provided to the Company	Fees (£)
Aon	Committee	Remuneration advice	None	32,404
MEIS	Committee	Data analysis	None	7,000
Stephenson Harwood LLP	Committee	Legal and remuneration advice	None	35,833
Ashurst	Committee	Legal advice	None	118,423

#### SHAREHOLDER VOTING AT PREVIOUS ANNUAL GENERAL MEETING (UNAUDITED)

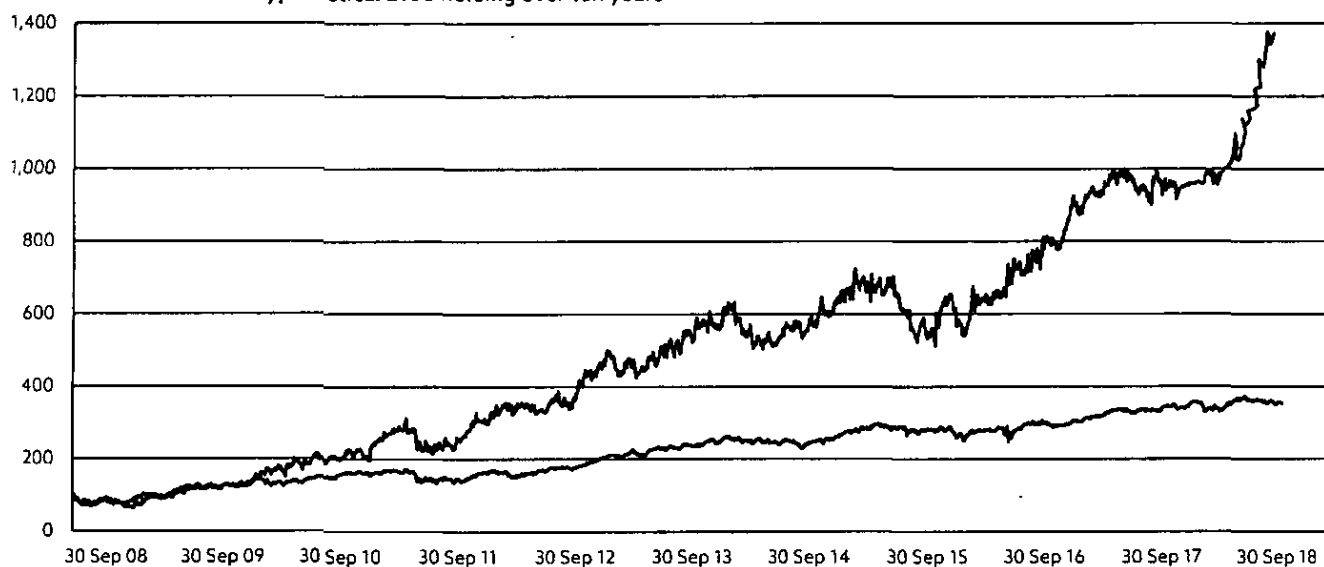
The Remuneration Committee's Annual Report ("the Report") and the Remuneration Committee's Report on Directors' Remuneration Policy ("the Policy") for the year ended 30 September 2017 was approved by shareholders at the AGM held on 17 January 2018, with the following votes being cast:

	Policy		Report	
Votes for	91,393,536	97.92%	90,383,863	96.84%
Votes against	1,941,428	2.08%	2,951,100	3.16%
Withheld	12,500		12,500	

#### ALIGNING PAY WITH PERFORMANCE (UNAUDITED)

The graph below shows the Total Shareholder Return ("TSR") performance of Diploma PLC for the ten-year period ended 30 September 2018 against the FTSE 250 Index as the Company is a member of this Index.

Growth in the value of a hypothetical £100 holding over ten years



— Diploma PLC — FTSE 250 (excluding Investment Trusts)

TSR is defined as the return on investment obtained from holding a company's shares over a period. It includes dividends paid, the change in the capital value of the shares and other payments to or by shareholders within the period.

#### CHIEF EXECUTIVE OFFICER REMUNERATION COMPARED WITH ANNUAL GROWTH IN TSR

Year	Name	Chief Executive Officer single figure of total remuneration (£'000)	Annual Bonus against maximum opportunity	Actual share award vesting	Annual growth in TSR
2018	John Nicholas <sup>1</sup>	14	—	—	+36%
2018	Richard Ingram <sup>2</sup>	235	—	—	+36%
2018	Bruce Thompson <sup>2</sup>	3,842	100%	99%	+36%
2017	Bruce Thompson	2,258	100%	89%	+24%
2016	Bruce Thompson	1,634	95%	45%	+36%
2015	Bruce Thompson	1,139	51%	25%	-1%
2014	Bruce Thompson	1,846	65%	61%	+8%
2013	Bruce Thompson	2,401	33%	100%	+42%
2012	Bruce Thompson	1,830	95%	100%	+54%
2011	Bruce Thompson	1,701	100%	100%	+16%
2010	Bruce Thompson	1,287	100%	100%	+71%
2009	Bruce Thompson	834	30%	91%	+21%

<sup>1</sup> John Nicholas is not eligible for an Annual Bonus or share award.

<sup>2</sup> These amounts are pro-rated for the period served as CEO, as explained on page 56.

# REMUNERATION COMMITTEE REPORT CONTINUED

## ANNUAL REPORT ON REMUNERATION CONTINUED

Set out below is the change over the prior year in base salary, benefits, pension, annual performance bonus and short-term remuneration of the Chief Executive Officer and the Group's senior management cadre.

	Change in base salary %	Change in pension %	Change in benefits %	Change in annual performance bonus %
Chief Executive Officer <sup>1</sup>	+3	+3	-	+3
Senior management cadre	+6	+3	-	+16

<sup>1</sup> Based solely on amounts paid to Bruce Thompson while he was Chief Executive Officer.

The Committee chose the senior management cadre for pay comparisons with the Chief Executive Officer as it provided the most closely aligned comparator group, considering the global and diverse nature of the Group's business.

## RELATIVE IMPORTANCE OF EXECUTIVE DIRECTOR REMUNERATION (UNAUDITED)

	2018 £m	2017 £m	Change £m
Total employee remuneration	92.7	86.4	+6.3
Total dividends paid	26.8	23.5	+3.3

## EXECUTIVE DIRECTORS' INTERESTS

### In options over shares

In respect of nil cost options granted under the PSP, the remuneration receivable by an Executive Director is calculated on the date that the options first vest. The remuneration of the Executive Director is the difference between the amount the Executive Director is required to pay to exercise the options to acquire the shares and the total value of the shares on the vesting date.

If the Executive Director chooses not to exercise the nil cost options on the vesting date (he may exercise the options at any time up to the day preceding the tenth anniversary of the date of grant), any subsequent increase or decrease in the amount realised will be due to movements in the underlying share price between the initial vesting date and the date of exercise of the option. This increase or decrease in value reflects an investment decision by the Executive Director and, as such, is not recorded as remuneration.

The nil cost options outstanding at 30 September 2018 and the movements during the year are as follows:

	Year of vesting	Options as at 1 Oct 2017	Exercised in year	Vested during the year	Options unexercised as at 30 Sep 2018	Exercise price <sup>4</sup>	Earliest normal exercise date	Expiry date
Bruce Thompson	2017	94,565	94,565	-	-	£1	Nov 2017	Dec 2024
	2018	-	-	193,212	193,212	£1	Nov 2018	Dec 2025
Nigel Lingwood	2017	61,056	61,056	-	-	£1	Nov 2017	Dec 2024
	2018	-	-	73,063	73,063	£1	Nov 2018	Dec 2025

<sup>1</sup> Bruce Thompson exercised 94,565 options on 24 November 2017, at a market price of 1,196p per share and the total proceeds before tax were £1,130,997.

<sup>2</sup> Nigel Lingwood exercised 61,056 options on 24 November 2017, at a market price of 1,196p per share and the total proceeds before tax were £730,230.

<sup>3</sup> On 24 November 2017, the aggregate number of shares received by the participants was reduced by 73,141 shares as part of arrangements under which the Company settled the PAYE liability that arose as a result of the exercise in full by the Executive Directors of options held over shares. The market price at that time was 1,196p.

<sup>4</sup> The closing price of an ordinary share on 30 September 2018 was 1,416p (2017: 1,059p).

<sup>5</sup> All awards have a notional exercise price of £1 per award.

### In ordinary shares

The Executive Directors' interests in ordinary shares of the Company were as follows:

	As at 30 Sep 2018 <sup>1</sup>			As at 30 Sep 2017		
	Ordinary shares	Options vested but unexercised	Interest in shares with performance measures	Ordinary shares	Options vested but unexercised	Interest in shares with performance measures
Bruce Thompson at 8 May 2018	516,450	-	270,557	570,000	94,565	198,893
Richard Ingram at 28 August 2018	-	-	126,550	-	-	-
Nigel Lingwood	180,000	73,063	101,329	200,000	61,056	128,391

<sup>1</sup> Bruce Thompson's interests are shown as at the date of his retirement from the Board on 8 May 2018 and are before vesting of the PSP option awards. Richard Ingram's interests are shown as at 28 August 2018 when he stood down from the Board.

Interests in ordinary shares include shares held through personal saving vehicles. As of 19 November 2018, there have been no changes to the interests in ordinary shares of the Company held by Nigel Lingwood.

At 30 September 2018 the ordinary shares held by Nigel Lingwood represented 789% of his base salary. The Committee has set a minimum shareholding guideline of 200% for the Executive Directors.



**CHAIRMAN AND NON-EXECUTIVE DIRECTORS' REMUNERATION**

Individual remuneration for the year ended 30 September was as follows:

	Total fees	
	2018 £000	2017 £000
John Nicholas	145	140
Charles Packshaw	55	54
Andy Smith	55	54
Anne Thorburn	55	54

The non-Executive Directors received a basic annual fee of £50,000 during the year and there were additional fees paid in 2018 of £5,000 (2017: £5,000) for chairing a Committee of the Board or for acting as Senior Independent Director. No additional fee for chairing a Committee of the Board is payable to the Chairman of the Company. The fees for non-Executive Directors are reviewed every year by the Board, taking into account their responsibilities and required time commitment. Following a review undertaken on 13 November 2018, the Board approved an increase of 3.0% in the Chairman's fee to £148,950 p.a. and in the basic annual fee paid to non-Executive Directors to £51,500. The additional fee for chairing a Committee of the Board will increase to £12,000 and for acting as Senior Independent Director will increase to £10,000. All these fee increases will take effect from 1 October 2018.

**CHAIRMAN AND NON-EXECUTIVE DIRECTORS' INTERESTS IN ORDINARY SHARES**

The non-Executive Directors' interests in ordinary shares of the Company at the start and at the end of the financial year were as follows:

	Interest in ordinary shares	
	As at 30 Sep 2018	As at 30 Sep 2017
John Nicholas	7,000	5,000
Charles Packshaw	1,500	1,500
Andy Smith	5,500	5,500
Anne Thorburn	3,000	3,000

**SENIOR EXECUTIVES BELOW THE BOARD (UNAUDITED)**

The policies and practices with regard to the remuneration of senior executives below the Executive Directors are generally treated consistently with the Executive Directors. These senior executives all have a significant portion of their reward package linked to performance. Annual bonuses are linked to short term financial targets which use similar performance metrics to the targets for the Executive Directors. Members of the Executive Management Committee ("EMC") participate in the Diploma PLC 2011 Performance Share Plan. Senior management outside the EMC participate in cash based long term incentive plans that are focused on the operating profit growth of their businesses over rolling three-year periods.

Set out below is a summary of the share-based awards outstanding at 30 September 2018 which have been granted to members of the EMC, including share awards which have vested during the year based on performance and share awards that have been granted both last year and during this year. The awards set out below were granted based on a face value limit that varied between 30% and 60% of base salary. No awards will vest unless the performance conditions set out on page 58 are achieved over a three-year measurement period.

**DIPLOMA PLC 2011 PERFORMANCE SHARE PLAN**

	Market price at date of award	Face value of the award at date of grant £000	End of performance period	Maturity date	Shares over which awards held at 1 Oct 2017	Shares over which awards granted during the year	Vested during the period	Lapsed during the period	Shares over which awards held at 30 Sep 2018
17 December 2015	730p	159	30 Sep 2018	30 Sep 2018	21,781	-	13,917	7,864	-
22 December 2016	997.5p	390	30 Sep 2019	30 Sep 2019	39,126	-	-	18,045	21,081
28 December 2017	1,221p	430	30 Sep 2020	30 Sep 2020	-	35,206	-	16,708	18,498

In November 2017, 18,961 nil cost options, in respect of awards which vested at 30 September 2017, were exercised by participants.

The Committee anticipates making similar awards to members of the EMC in December 2018.

## DIRECTORS' REPORT

This section contains information which the Directors are required by law and regulation to include within the Annual Report & Accounts. The Directors who held office during the year are set out on pages 36 and 37.

### SHAREHOLDERS

#### Incorporation and principal activity

Diploma PLC is domiciled in England and registered in England and Wales under Company Number 3899848. At the date of this Report there were 113,239,555 ordinary shares of 5p each in issue, all of which are fully paid up and quoted on the London Stock Exchange.

The principal activity of the Group is the supply of specialised technical products and services. A description and review of the activities of the Group during the financial year and an indication of future developments is set out on pages 4 to 35; the Strategic Report on pages 1 to 35 incorporates the requirements of the Companies Act 2006 ("the Act").

#### Annual General Meeting

The Annual General Meeting ("AGM") will be held at midday on Wednesday, 16 January 2019 in the Brewers Hall, Aldermanbury Square, London EC2V 7HR. The Notice of the AGM, which is a separate document, will be sent to all shareholders and will be published on the Diploma PLC website.

#### Substantial shareholdings

At 16 November 2018, the Company had been notified of the following interests amounting to 3% or more of the voting rights in its ordinary share capital:

	Percentage of ordinary share capital
Standard Life Aberdeen plc	8.01
Mondrian Investment Partners Ltd	7.26
Mawer Investment Management Ltd	6.49
Royal London Group	5.44
Blackrock, Inc	3.30
Fidelity Management & Research Co	3.16
Norges Bank Investment Management	3.03

As far as the Directors are aware, there were no other interests above 3% of the issued ordinary share capital.

#### Share capital

The rights attaching to the Company's ordinary shares, as well as the powers of the Company's Directors, are set out in the Company's Articles of Association, copies of which can be obtained from the Group Company Secretary and are available on the Company's website.

The Company is not aware of any agreements between shareholders that may result in restrictions on the transfers of securities and/or voting rights. No person holds securities in the Company carrying special rights with regard to control of the Company. The Company's Articles of Association may be amended by special resolution of the Company's shareholders.

#### Restrictions on transfer of shares

The Directors may refuse to register a transfer of a certificated share that is not fully paid, provided that the refusal does not prevent dealings in shares in the Company from taking place on an open and proper basis, or where the Company has lien over that share. The Directors may also refuse to register a transfer of a certificated share, unless the instrument of transfer is:

- (i) lodged, duly stamped (if necessary), at the registered office of the Company or any other place as the Board may decide accompanied by the certificate for the share(s) to be transferred and/or such other evidence as the Directors may reasonably require to show the right of the transferor to make the transfer;
- (ii) in respect of only one class of shares; (iii) in favour of a person who is not a minor, infant, bankrupt or a person of unsound mind; or (iv) in favour of not more than four persons jointly.

Transfers of uncertificated shares must be carried out using CREST and the Directors can refuse to register a transfer of an uncertificated share in accordance with the regulations governing the operation of CREST.

Participants in the Company's Performance Share Plan ("the PSP"), who have yet to meet shareholding guidelines, have vested PSP shares held in trust until the earlier occurrence of them meeting their required shareholder guideline or for a period of two years, during which period these shares cannot be transferred to them. There are no other restrictions on the transfer of ordinary shares in the Company except certain restrictions which may from time to time be imposed by laws and regulations (for example insider trading laws); or where a shareholder with at least a 0.25% interest in the Company's certificated shares has been served with a disclosure notice and has failed to provide the Company with information concerning interests in those shares.

#### Shares held by the Diploma PLC Employee Benefit Trust

While ordinary shares are held within the Diploma PLC Employee Benefit Trust, the voting rights in respect of those shares are exercisable by the Trustees in accordance with their fiduciary duties. The Trustees of the Diploma PLC Employee Benefit Trust also waive dividends on all shares held for the purposes of the Company's long term incentive arrangements.

#### Share allotment

A general allotment power and a limited power to allot shares in specific circumstances for cash, otherwise than pro-rata to existing shareholders, were given to the Directors by resolutions approved at the AGM of the Company held on 17 January 2018. In the year ended 30 September 2018, the Company has not allotted any shares. These powers will expire at the conclusion of the 2019 AGM and resolutions to renew the Directors' powers are therefore included within the Notice of the AGM in 2019.

#### Authority to make market purchases of own shares

An authority to make market purchases of shares was given to the Directors by a special resolution at the AGM of the Company held on 17 January 2018. In the year to 30 September 2018 the Company has not acquired any of its own shares. This authority will expire at the conclusion of the 2019 AGM and a resolution to renew the authority is therefore included within the Notice of the AGM in 2019.

#### Disclosures required under Listing Rule 9.8.4R

There is no information to be disclosed by the Company in respect of Listing Rule 9.8.4R, except for:

- Long Term Incentive Plan (details of the LTIP awarded to Richard Ingram on 15 May 2018 in connection with his appointment as Chief Executive Officer is set out on page 56 of the Remuneration Committee Report. This award lapsed on 28 August 2018 when Richard Ingram stood down as Chief Executive Officer and left the Company; and
- The Employee Benefit Trust has waived dividends on all shares held.

**FINANCIAL****Results and dividends**

The profit for the financial year attributable to shareholders was £53.8m (2017: £47.5m). The Directors recommend a final dividend of 17.8p per ordinary share (2017: 16.0p), to be paid, if approved, on 23 January 2019. This, together with the interim dividend of 7.7p (2017: 7.0p) per ordinary share paid on 13 June 2018 amounts to 25.5p for the year (2017: 23.0p).

The results are shown more fully in the consolidated financial statements on pages 66 to 93 and summarised in the Finance Review on pages 26 to 29.

**Auditor**

Each of the persons who is a Director at the date of approval of this Annual Report & Accounts confirms that so far as the Director is aware, there is no relevant audit information of which the Company's Auditor is unaware; and the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's Auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of Section 418 of the Companies Act 2006.

PricewaterhouseCoopers LLP ("PwC") has expressed its willingness to continue in office as Independent Auditor and a resolution to re-appoint PwC will be proposed at the Annual General Meeting to be held on 16 January 2019.

**Directors' assessment of going concern**

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 1 to 35. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Finance Review on pages 26 to 29. In addition, pages 79 to 81 of the Annual Report & Accounts include the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

The Group has considerable financial resources, together with a broad spread of customers and suppliers across different geographic areas and sectors, often secured with longer term agreements. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully as described further on pages 30 to 33.

The Group also has a committed multi-currency revolving bank facility of £30.0m with an accordion option to increase the committed facility by a further £30.0m up to a maximum of £60.0m. This facility expires on 31 May 2020, with an option to extend the facility to 31 May 2022. At 30 September 2018, the Group had cash funds of £36.0m and had no borrowings.

After making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report & Accounts.

**Statement of Directors' responsibilities for preparing the financial statements**

The Directors are responsible for preparing the Annual Report & Accounts, including the Group and Parent Company financial statements, in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law the Directors are required to prepare Group financial statements in accordance with IFRS as adopted by the European Union ("EU") and Article 4 of the IAS Regulations and have elected

to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Standards (UK Accounting Standards) including FRS101 ("Reduced Disclosures Framework").

The Group financial statements are required by law and IFRS as adopted by the EU, to present fairly the financial position and the performance of the Group; the Act provides in relation to such financial statements, that references in the relevant part of that Act to financial statements giving a true and fair view, are references to their achieving a fair presentation.

In preparing each of the Group and Parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- for the Group financial statements, state whether they have been prepared in accordance with IFRS, as adopted by the EU;
- for the Parent Company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the Parent Company financial statements; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that the financial statements comply with the Act. They are also responsible for safeguarding the assets of the Parent 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 UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

**Directors' Responsibility Statement**

The Directors confirm that to the best of their knowledge:

- the Group's consolidated financial statements, prepared in accordance with IFRS as adopted by the EU and the Parent Company financial statements, prepared in accordance with UK Accounting Standards, give a true and fair view of the assets, liabilities, financial position and profit of the Group and Parent Company and the undertakings included in the consolidation taken as a whole;
- the Annual Report & Accounts includes a fair review of the development and performance of the business and the position of the Group and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties faced by the Group; and
- the Annual Report & Accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy.

This responsibility statement was approved by the Board of Directors on 19 November 2018 and is signed on its behalf by:

  
NP Lingwood  
Group Finance Director

  
JE Nicholas  
Chairman

Registered office:  
12 Charterhouse Square  
London  
EC1M 6AX

## CONSOLIDATED INCOME STATEMENT

FOR THE YEAR ENDED 30 SEPTEMBER 2018

	Note	2018 £m	2017 £m
<b>Revenue</b>	3,4	<b>485.1</b>	451.9
Cost of sales		(312.2)	(290.8)
<b>Gross profit</b>		<b>172.9</b>	161.1
Distribution costs		(10.8)	(10.6)
Administration costs		(88.9)	(82.0)
<b>Operating profit</b>	3	<b>73.2</b>	68.5
Financial expense, net	6	(0.5)	(1.7)
<b>Profit before tax</b>		<b>72.7</b>	66.8
Tax expense	7	(18.3)	(18.6)
<b>Profit for the year</b>		<b>54.4</b>	48.2
Attributable to:			
Shareholders of the Company		53.8	47.5
Minority interests	21	0.6	0.7
	-	<b>54.4</b>	48.2
<b>Earnings per share</b>			
Basic and diluted earnings	9	47.5p	42.0p

### ALTERNATIVE PERFORMANCE MEASURES (NOTE 2)

	Note	2018 £m	2017 £m
Operating profit		73.2	68.5
Add: Acquisition related charges	11	9.6	9.7
Add: CEO transition costs	28	2.1	-
<b>Adjusted operating profit</b>	3,4	<b>84.9</b>	78.2
Deduct: Interest expense	6	(0.1)	(0.7)
<b>Adjusted profit before tax</b>		<b>84.8</b>	77.5
<b>Adjusted earnings per share</b>	9	<b>56.4p</b>	49.8p

The notes on pages 70 to 93 form part of these consolidated financial statements.

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

	Note	2018 £m	2017 £m
<b>Profit for the year</b>		<b>54.4</b>	<b>48.2</b>
<b>Items that will not be reclassified to the Consolidated Income Statement</b>			
Actuarial (losses)/gains in the defined benefit pension schemes	25	(1.0)	7.1
Deferred tax on items that will not be reclassified	7,14	0.2	(1.3)
		<b>(0.8)</b>	<b>5.8</b>
<b>Items that may be reclassified to Consolidated Income Statement</b>			
Exchange rate gains/(losses) on foreign currency net investments		0.1	(0.8)
Gains/(losses) on fair value of cash flow hedges	19	0.7	(1.0)
Net changes to fair value of cash flow hedges transferred to the Consolidated Income Statement	19	0.9	(0.2)
Deferred tax on items that may be reclassified	7,14	(0.4)	0.3
		<b>1.3</b>	<b>(1.7)</b>
<b>Total Comprehensive Income for the year</b>		<b>54.9</b>	<b>52.3</b>
Attributable to:			
Shareholders of the Company		<b>54.2</b>	<b>51.6</b>
Minority interests		<b>0.7</b>	<b>0.7</b>
		<b>54.9</b>	<b>52.3</b>

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

	Note	Share capital £m	Translation reserve £m	Hedging reserve £m	Retained earnings £m	Shareholders' equity £m	Minority interests £m	Total equity £m
<b>At 1 October 2016</b>		5.7	30.5	0.2	197.1	<b>233.5</b>	4.3	<b>237.8</b>
Total Comprehensive Income		-	(0.8)	(0.9)	53.3	<b>51.6</b>	0.7	<b>52.3</b>
Share-based payments	5	-	-	-	0.8	<b>0.8</b>	-	<b>0.8</b>
Tax on items recognised directly in equity	7	-	-	-	0.3	<b>0.3</b>	-	<b>0.3</b>
Notional purchase of own shares		-	-	-	(0.7)	<b>(0.7)</b>	-	<b>(0.7)</b>
Dividends	8,21	-	-	-	(23.5)	<b>(23.5)</b>	(0.2)	<b>(23.7)</b>
<b>At 30 September 2017</b>		5.7	29.7	(0.7)	227.3	<b>262.0</b>	4.8	<b>266.8</b>
Total Comprehensive Income		-	0.1	1.2	52.9	<b>54.2</b>	0.7	<b>54.9</b>
Share-based payments	5	-	-	-	1.0	<b>1.0</b>	-	<b>1.0</b>
Minority interests acquired	21	-	-	-	2.5	<b>2.5</b>	(2.5)	-
Minority interest contribution	21	-	-	-	-	-	0.3	<b>0.3</b>
Tax on items recognised directly in equity	7	-	-	-	0.5	<b>0.5</b>	-	<b>0.5</b>
Notional purchase of own shares		-	-	-	(2.2)	<b>(2.2)</b>	-	<b>(2.2)</b>
Dividends	8,21	-	-	-	(26.8)	<b>(26.8)</b>	(0.2)	<b>(27.0)</b>
<b>At 30 September 2018</b>		5.7	29.8	0.5	255.2	<b>291.2</b>	3.1	<b>294.3</b>

The notes on pages 70 to 93 form part of these consolidated financial statements.

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION

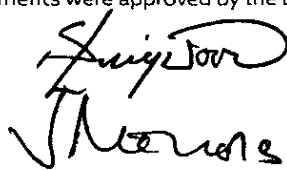
AS AT 30 SEPTEMBER 2018

	Note	2018 £m	2017 £m
<b>Non-current assets</b>			
Goodwill	10	128.5	122.8
Acquisition intangible assets	11	53.6	54.0
Other intangible assets	11	1.8	0.7
Investment	12	0.7	0.7
Property, plant and equipment	13	23.0	22.6
Deferred tax assets	14	0.3	0.2
		<b>207.9</b>	<b>201.0</b>
<b>Current assets</b>			
Inventories	15	82.9	73.2
Trade and other receivables	16	77.6	68.9
Cash and cash equivalents	18	36.0	22.3
		<b>196.5</b>	<b>164.4</b>
<b>Current liabilities</b>			
Trade and other payables	17	(80.5)	(69.7)
Current tax liabilities	7	(4.8)	(4.0)
Other liabilities	20	(5.6)	(2.5)
		<b>(90.9)</b>	<b>(76.2)</b>
<b>Net current assets</b>		<b>105.6</b>	<b>88.2</b>
<b>Total assets less current liabilities</b>		<b>313.5</b>	<b>289.2</b>
<b>Non-current liabilities</b>			
Retirement benefit obligations	25	(10.5)	(9.9)
Other liabilities	20	-	(4.1)
Deferred tax liabilities	14	(8.7)	(8.4)
<b>Net assets</b>		<b>294.3</b>	<b>266.8</b>
<b>Equity</b>			
Share capital		5.7	5.7
Translation reserve		29.8	29.7
Hedging reserve		0.5	(0.7)
Retained earnings		255.2	227.3
<b>Total shareholders' equity</b>		<b>291.2</b>	<b>262.0</b>
Minority interests	21	3.1	4.8
<b>Total equity</b>		<b>294.3</b>	<b>266.8</b>

The consolidated financial statements were approved by the Board of Directors on 19 November 2018 and signed on its behalf by:

NP Lingwood  
Group Finance Director

JE Nicholas  
Chairman



The notes on pages 70 to 93 form part of these consolidated financial statements.

# CONSOLIDATED CASH FLOW STATEMENT

FOR THE YEAR ENDED 30 SEPTEMBER 2018

	Note	2018 £m	2017 £m
<b>Operating profit</b>		<b>73.2</b>	<b>68.5</b>
Acquisition related charges	23	9.6	9.7
CEO transition costs, unpaid	23,28	1.3	-
Non-cash items	23	5.3	5.1
Increase in working capital	23	(5.1)	(4.0)
<b>Cash flow from operating activities</b>	<b>23</b>	<b>84.3</b>	<b>79.3</b>
Interest paid, net		-	(0.4)
Tax paid		(19.0)	(19.3)
<b>Net cash from operating activities</b>		<b>65.3</b>	<b>59.6</b>
<b>Cash flow from investing activities</b>			
Acquisition of businesses (including expenses, net of cash acquired)	22	(18.1)	(19.5)
Deferred consideration paid	20	(0.3)	(0.6)
Proceeds from sale of business (net of expenses)	22	4.0	-
Purchase of property, plant and equipment	13	(5.3)	(3.1)
Purchase of other intangible assets	11	(1.3)	(0.2)
Proceeds from sale of property, plant and equipment		-	0.1
<b>Net cash used in investing activities</b>		<b>(21.0)</b>	<b>(23.3)</b>
<b>Cash flow from financing activities</b>			
Acquisition of minority interests	20	(2.0)	-
Dividends paid to shareholders	8	(26.8)	(23.5)
Dividends paid to minority interests	21	(0.2)	(0.2)
Purchase of own shares by Employee Benefit Trust		(1.2)	-
Notional purchase of own shares on exercise of share options		(1.0)	(0.7)
Repayment of borrowings, net	24	-	(10.0)
<b>Net cash used in financing activities</b>		<b>(31.2)</b>	<b>(34.4)</b>
<b>Net increase in cash and cash equivalents</b>		<b>13.1</b>	<b>1.9</b>
Cash and cash equivalents at beginning of year		22.3	20.6
Effect of exchange rates on cash and cash equivalents		0.6	(0.2)
<b>Cash and cash equivalents at end of year</b>	<b>18</b>	<b>36.0</b>	<b>22.3</b>

## ALTERNATIVE PERFORMANCE MEASURES (NOTE 2)

	Note	2018 £m	2017 £m
Net increase in cash and cash equivalents		13.1	1.9
Add: Dividends paid to shareholders	8	26.8	23.5
Dividends paid to minority interests	21	0.2	0.2
Acquisition of businesses (including expenses, net of cash acquired)	22	18.1	19.5
Acquisition of minority interests	20	2.0	-
Deferred consideration paid	20	0.3	0.6
Repayment of borrowings, net	24	-	10.0
<b>Free cash flow</b>		<b>60.5</b>	<b>55.7</b>
<b>Cash funds</b>	<b>24</b>	<b>36.0</b>	<b>22.3</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### 1. GENERAL INFORMATION

Diploma PLC is a public limited company registered and domiciled in England and Wales and listed on the London Stock Exchange. The address of the registered office is 12 Charterhouse Square, London EC1M 6AX. The consolidated financial statements comprise the Company and its subsidiaries (together referred to as "the Group") and were authorised by the Directors for publication on 19 November 2018. These statements are presented in UK sterling, with all values rounded to the nearest 100,000, except where otherwise indicated.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs"), as adopted by the European Union ("EU") and in accordance with the Companies Act 2006, as applicable to companies reporting under IFRS. The financial statements of the Parent Company, Diploma PLC, have been prepared in accordance with FRS101 "Reduced Disclosure Framework" and are set out in a separate section of the Annual Report & Accounts on pages 94 and 95.

#### 2. ALTERNATIVE PERFORMANCE MEASURES

The Group uses a number of alternative (non-Generally Accepted Accounting Practice ("non-GAAP")) financial measures which are not defined within IFRS. The Directors use these measures for internal management reporting in order to assess the operational performance of the Group on a comparable basis, and as such these measures should be considered alongside the IFRS measures. The following non-GAAP measures are referred to in this Annual Report & Accounts:

##### 2.1 Adjusted operating profit

At the foot of the Consolidated Income Statement, "adjusted operating profit" is defined as operating profit before amortisation and impairment of acquisition intangible assets, acquisition expenses, adjustments to deferred consideration (collectively, "acquisition related charges"), the costs of a material restructuring (including the incremental cost related directly to the change of the Chief Executive Officer in 2018) or rationalisation of operations and the profit or loss relating to the sale of businesses or property. The Directors believe that adjusted operating profit is an important measure of the operational performance of the Group.

##### 2.2 Adjusted profit before tax

At the foot of the Consolidated Income Statement, "adjusted profit before tax" is separately disclosed, being defined as adjusted operating profit, after finance expenses (but before fair value remeasurements under IAS39 in respect of future purchases of minority interests) and before tax. The Directors believe that adjusted profit before tax is an important measure of the operational performance of the Group.

##### 2.3 Adjusted earnings per share

"Adjusted earnings per share" ("adjusted EPS") is calculated as the total of adjusted profit before tax, less income tax costs, but including the tax impact on the items included in the calculation of adjusted profit, less profit attributable to minority interests, divided by the weighted average number of ordinary shares in issue during the year. The Directors believe that adjusted EPS provides an important measure of the earning capacity of the Group.

##### 2.4 Free cash flow

At the foot of the Consolidated Cash Flow Statement, "free cash flow" is reported, being defined as net cash flow from operating activities, after net capital expenditure on fixed assets and including proceeds received from business disposals, but before expenditure on business combinations/investments and dividends paid to both minority shareholders and the Company's shareholders. The Directors believe that free cash flow gives an important measure of the cash flow of the Group, available for future investment or distribution to shareholders.

##### 2.5 Trading capital employed and ROATCE

In the Sector analysis in note 3, "trading capital employed" is reported, being defined as net assets less cash and cash equivalents and after adding back: borrowings; retirement benefit obligations; deferred tax; and acquisition liabilities in respect of future purchases of minority interests and deferred consideration. Adjusted trading capital employed is reported as being trading capital employed plus goodwill and acquisition related charges previously written off (net of deferred tax on acquisition intangible assets). Return on adjusted trading capital employed ("ROATCE") at the Group and Sector level is defined as the adjusted operating profit, divided by adjusted trading capital employed and adjusted for the full year effect of major acquisitions and disposals. The Directors believe that ROATCE is an important measure of the profitability of the Group.

#### 3. BUSINESS SECTOR ANALYSIS

The Chief Operating Decision Maker ("CODM") for the purposes of IFRS8 is the Chief Executive Officer (or interim Executive Chairman). The financial performance of the Sectors are reported to the CODM on a monthly basis and this information is used to allocate resources on an appropriate basis.

For management reporting purposes, the Group is organised into three main reportable business Sectors: Life Sciences, Seals and Controls. These Sectors form the basis of the primary reporting format disclosures below. The principal activities of each of these Sectors is described in the Strategic Report on pages 1 to 25 (unaudited). Sector revenue represents revenue from external customers; there is no inter-Sector revenue. Sector results, assets and liabilities include items directly attributable to a Sector, as well as those that can be allocated on a reasonable basis.

Sector assets exclude cash and cash equivalents, deferred tax assets and corporate assets that cannot be allocated on a reasonable basis to a business Sector. Sector liabilities exclude borrowings, retirement benefit obligations, deferred tax liabilities, acquisition liabilities and corporate liabilities that cannot be allocated on a reasonable basis to a business Sector. These items are shown collectively in the following analysis as "unallocated assets" and "unallocated liabilities", respectively.



## 3. BUSINESS SECTOR ANALYSIS CONTINUED

	Life Sciences		Seals		Controls		Group	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
Revenue – existing	134.7	125.9	208.0	195.3	137.3	130.7	480.0	451.9
Revenue – acquisitions	–	–	–	–	5.1	–	5.1	–
<b>Revenue</b>	<b>134.7</b>	<b>125.9</b>	<b>208.0</b>	<b>195.3</b>	<b>142.4</b>	<b>130.7</b>	<b>485.1</b>	<b>451.9</b>
Adjusted operating profit – existing	23.9	23.3	36.0	31.9	24.6	23.0	84.5	78.2
Adjusted operating profit – acquisitions	–	–	–	–	0.4	–	0.4	–
<b>Adjusted operating profit</b>	<b>23.9</b>	<b>23.3</b>	<b>36.0</b>	<b>31.9</b>	<b>25.0</b>	<b>23.0</b>	<b>84.9</b>	<b>78.2</b>
Acquisition related charges	(2.4)	(3.2)	(5.0)	(5.5)	(2.2)	(1.0)	(9.6)	(9.7)
CEO transition costs	–	–	–	–	–	–	(2.1)	–
<b>Operating profit</b>	<b>21.5</b>	<b>20.1</b>	<b>31.0</b>	<b>26.4</b>	<b>22.8</b>	<b>22.0</b>	<b>73.2</b>	<b>68.5</b>

	Life Sciences		Seals		Controls		Group	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
Operating assets	43.5	42.2	80.1	74.6	59.3	48.1	182.9	164.9
Investment	–	–	0.7	0.7	–	–	0.7	0.7
Goodwill	59.0	59.5	40.3	39.9	29.2	23.4	128.5	122.8
Acquisition intangible assets	12.9	15.4	21.8	27.0	18.9	11.6	53.6	54.0
	115.4	117.1	142.9	142.2	107.4	83.1	365.7	342.4
Unallocated assets:								
– Deferred tax assets							0.3	0.2
– Cash and cash equivalents							36.0	22.3
– Corporate assets							2.4	0.5
<b>Total assets</b>	<b>115.4</b>	<b>117.1</b>	<b>142.9</b>	<b>142.2</b>	<b>107.4</b>	<b>83.1</b>	<b>404.4</b>	<b>365.4</b>
Operating liabilities	(21.6)	(21.3)	(32.2)	(26.6)	(25.5)	(21.1)	(79.3)	(69.0)
Unallocated liabilities:								
– Deferred tax liabilities							(8.7)	(8.4)
– Retirement benefit obligations							(10.5)	(9.9)
– Acquisition liabilities							(5.6)	(6.6)
– Corporate liabilities							(6.0)	(4.7)
<b>Total liabilities</b>	<b>(21.6)</b>	<b>(21.3)</b>	<b>(32.2)</b>	<b>(26.6)</b>	<b>(25.5)</b>	<b>(21.1)</b>	<b>(110.1)</b>	<b>(98.6)</b>
<b>Net assets</b>	<b>93.8</b>	<b>95.8</b>	<b>110.7</b>	<b>115.6</b>	<b>81.9</b>	<b>62.0</b>	<b>294.3</b>	<b>266.8</b>

## ALTERNATIVE PERFORMANCE MEASURES (NOTE 2)

	Life Sciences		Seals		Controls		Group	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
<b>Net assets</b>	<b>93.8</b>	<b>95.8</b>	<b>110.7</b>	<b>115.6</b>	<b>81.9</b>	<b>62.0</b>	<b>294.3</b>	<b>266.8</b>
Add/(deduct):								
– Deferred tax, net							8.4	8.2
– Retirement benefit obligations							10.5	9.9
– Acquisition liabilities							5.6	6.6
– Cash and cash equivalents							(36.0)	(22.3)
<b>Reported trading capital employed</b>							<b>282.8</b>	<b>269.2</b>
– Historic goodwill and acquisition related charges, net of deferred tax	31.4	28.8	33.0	28.1	10.2	9.4	74.6	66.3
<b>Adjusted trading capital employed</b>	<b>125.2</b>	<b>124.6</b>	<b>143.7</b>	<b>143.7</b>	<b>92.1</b>	<b>71.4</b>	<b>357.4</b>	<b>335.5</b>
Pro-forma adjusted operating profit <sup>1</sup>	23.9	24.6	36.3	32.8	27.4	23.0	87.6	80.4
<b>ROATCE</b>	<b>19.1%</b>	<b>19.7%</b>	<b>25.3%</b>	<b>22.8%</b>	<b>29.8%</b>	<b>32.2%</b>	<b>24.5%</b>	<b>24.0%</b>

<sup>1</sup> After annualisation of adjusted operating profit of acquisitions and disposals.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 30 SEPTEMBER 2018

### 3. BUSINESS SECTOR ANALYSIS CONTINUED

#### Other Sector information

	Life Sciences		Seals		Controls		Group	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
Capital expenditure	3.5	2.0	2.0	1.1	1.1	0.2	6.6	3.3
Depreciation and amortisation	2.4	2.2	1.8	1.9	0.6	0.6	4.8	4.7

### 4. GEOGRAPHIC SEGMENT ANALYSIS BY ORIGIN

	Revenue		Adjusted operating profit		Non-current assets <sup>1</sup>		Trading capital employed		Capital expenditure	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
United Kingdom	130.2	118.4	23.5	20.6	54.1	42.3	79.2	60.1	0.6	0.3
Rest of Europe	115.2	112.8	17.6	17.2	57.0	58.6	76.9	76.9	1.5	0.6
North America	202.3	188.3	39.5	36.3	70.5	70.9	97.1	99.9	4.0	1.9
Rest of World	37.4	32.4	4.3	4.1	25.3	28.3	29.6	32.3	0.5	0.5
	485.1	451.9	84.9	78.2	206.9	200.1	282.8	269.2	6.6	3.3

<sup>1</sup> Non-current assets exclude investments and deferred tax assets.

### 5. GROUP EMPLOYEE COSTS

#### Average number of employees

	2018	2017
Life Sciences	420	382
Seals	857	830
Controls	471	430
Corporate	17	16
<b>Number of employees - average</b>	<b>1,765</b>	<b>1,658</b>
<b>Number of employees - year end</b>	<b>1,803</b>	<b>1,728</b>

#### Group employee costs, including key management

	2018 £m	2017 £m
Wages and salaries	81.2	75.7
Social security costs	7.4	7.1
Pension costs	3.1	2.8
Share-based payments	1.0	0.8
	92.7	86.4

#### Key management short term remuneration, including Directors

	2018 £m	2017 £m
Salaries and short term employee benefits	3.6	3.2
Pension costs	0.3	0.3
Share-based payments	1.0	0.8
	4.9	4.3

The Group considers key management personnel as defined in IAS24 "Related Party Disclosures" to be the Directors of the Company and the members of the Executive Management Committee ("EMC") as set out on pages 36 and 37.

The Executive Directors' remuneration and their interests in shares of the Company are given on pages 56 to 62 in the Remuneration Committee Report. The EMC's interests in the Group's LTIP is set out on page 63. The charge for share-based payments of £1.0m (2017: £0.8m) relates to the Group's LTIP, described in the Remuneration Committee Report.

#### Directors' short term remuneration

	2018 £m	2017 £m
Non-executive Directors	0.3	0.3
Executive Directors	2.0	1.9
	2.3	2.2

## 6. FINANCIAL EXPENSE, NET

	2018 £m	2017 £m
<b>Interest (expense)/income and similar charges</b>		
- bank facility and commitment fees	(0.1)	(0.3)
- interest income on bank deposits	0.1	-
- interest expense on bank borrowings	-	(0.1)
- notional interest expense on the defined benefit pension scheme (note 25b)	(0.1)	(0.3)
<b>Net interest expense and similar charges</b>	(0.1)	(0.7)
- fair value remeasurement of put options (note 20)	(0.4)	(1.0)
<b>Financial expense, net</b>	(0.5)	(1.7)

The fair value remeasurement of £0.4m (2017: £1.0m) comprises £0.2m (2017: £0.5m) that relates to the unwinding of the discount on the liability for future purchases of minority interests and a movement in the fair value of the put options of £0.2m debit (2017: £0.5m debit).

## 7. TAX EXPENSE

	2018 £m	2017 £m
<b>Current tax</b>		
The tax charge is based on the profit for the year and comprises:		
UK corporation tax	3.9	3.7
Overseas tax	16.1	17.2
	20.0	20.9
Adjustments in respect of prior year:		
UK corporation tax	-	(0.5)
Overseas tax	(0.1)	0.2
<b>Total current tax</b>	19.9	20.6
<b>Deferred tax</b>		
The net deferred tax credit based on the origination and reversal of timing differences comprises:		
United Kingdom	(0.4)	(1.9)
Overseas	(1.2)	(0.1)
<b>Total deferred tax</b>	(1.6)	(2.0)
<b>Total tax on profit for the year</b>	18.3	18.6

In addition to the above credit for deferred tax included in the Consolidated Income Statement, a net deferred tax debit relating to the retirement benefit scheme and cash flow hedges of £0.2m was debited (2017: £1.0m debit) directly to the Consolidated Statement of Comprehensive Income. A further £0.5m of current tax (2017: £0.3m) was credited to the Consolidated Statement of Changes in Equity which relates to share-based payments made during the year.

### Factors affecting the tax charge for the year

The difference between the total tax charge calculated by applying the effective rate of UK corporation tax of 19.0% to the profit before tax of £72.7m and the amount set out above is as follows:

	2018 £m	2017 £m
<b>Profit before tax</b>	72.7	66.8
Tax on profit at UK effective corporation tax rate of 19.0% (2017: 19.5%)	13.8	13.0
Effects of:		
- higher tax rates on overseas earnings	4.0	5.3
- adjustments to current tax charge in respect of previous years	(0.1)	(0.3)
- other permanent differences	0.6	0.6
<b>Total tax on profit for the year</b>	18.3	18.6

The Group earns its profits in the UK and overseas. The UK corporation tax rate was reduced from 20.0% to 19.0% on 1 April 2017. As the Group prepares its consolidated financial statements for the year to 30 September, the effective tax rate for UK corporation tax in respect of the year ended 30 September 2018 was 19.0% (2017: 19.5%) and this rate has been used for tax on profit in the above reconciliation.

The reduction in the effective rate of taxation reflects the impact from the reduction in the US Federal corporate income tax rate to 21% from 35%, effective from 1 January 2018. There was no material impact from the revaluation of US deferred tax balances at the reduced tax rate. The Group's US businesses account for ca. 26% of Group revenues and adjusted operating profit before tax.

The Group's net overseas tax rate is higher than that in the UK, primarily because profits earned in the US, Canada and Australia are taxed at higher rates than the UK.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### 7. TAX EXPENSE CONTINUED

The UK deferred tax assets and liabilities at 30 September 2018 have been calculated based on the future UK corporation tax rate of 17.0%, as substantively enacted at 30 September 2018.

At 30 September 2018, the Group had outstanding tax liabilities of £4.8m (2017: £4.0m) of which £2.1m related to UK tax liabilities and £2.7m related to overseas tax liabilities. These amounts are expected to be paid within the next financial year.

#### 8. DIVIDENDS

	2018 pence per share	2017 pence per share	2018 £m	2017 £m
Interim dividend, paid in June	7.7	7.0	8.7	7.9
Final dividend of the prior year, paid in January	16.0	13.8	18.1	15.6
	23.7	20.8	26.8	23.5

The Directors have proposed a final dividend in respect of the current year of 17.8p per share (2017: 16.0p), which will be paid on 23 January 2019, subject to approval of shareholders at the Annual General Meeting on 16 January 2019. The total dividend for the current year, subject to approval of the final dividend, will be 25.5p per share (2017: 23.0p).

The Diploma PLC Employee Benefit Trust holds 100,368 (2017: 92,898) shares, which are ineligible for dividends.

#### 9. EARNINGS PER SHARE

##### Basic and diluted earnings per share

Basic and diluted earnings per ordinary 5p share are calculated on the basis of the weighted average number of ordinary shares in issue during the year of 113,140,435 (2017: 113,133,341) and the profit for the year attributable to shareholders of £53.8m (2017: £47.5m). There are no potentially dilutive shares. Further description of the Company's share capital is set out in note e to the Parent Company Financial Statements on page 95.

##### Adjusted earnings per share

Adjusted EPS, which is defined in note 2, is calculated as follows:

	2018 pence per share	2017 pence per share	2018 £m	2017 £m
Profit before tax			72.7	66.8
Tax expense			(18.3)	(18.6)
Minority interests			(0.6)	(0.7)
<b>Earnings for the year attributable to shareholders of the Company</b>	<b>47.5</b>	<b>42.0</b>	<b>53.8</b>	<b>47.5</b>
Acquisition related charges	8.4	8.6	9.6	9.7
Fair value remeasurement of put options	0.4	0.9	0.4	1.0
CEO transition costs	1.8	-	2.1	-
Tax effects on above adjustments	(1.7)	(1.7)	(2.0)	(1.9)
<b>Adjusted earnings</b>	<b>56.4</b>	<b>49.8</b>	<b>63.9</b>	<b>56.3</b>

#### 10. GOODWILL

	Life Sciences £m	Seals £m	Controls £m	Total £m
At 1 October 2016	52.8	39.1	23.3	115.2
Acquisitions	6.1	1.4	-	7.5
Exchange adjustments	0.6	(0.6)	0.1	0.1
At 30 September 2017	59.5	39.9	23.4	122.8
Acquisitions (note 22)	-	-	5.7	5.7
Exchange adjustments	(0.5)	0.4	0.1	-
<b>At 30 September 2018</b>	<b>59.0</b>	<b>40.3</b>	<b>29.2</b>	<b>128.5</b>

The Group tests goodwill for impairment at least once a year. For the purposes of impairment testing, goodwill is allocated to each of the Group's three operating Sectors. This reflects the lowest level within the Group at which goodwill is monitored by management and reflects the Group's strategy of acquiring businesses to drive synergies across a Sector, rather than within an individual business. The impairment test requires a "value in use" valuation to be prepared for each Sector using discounted cash flow forecasts. The cash flow forecasts are based on a combination of annual budgets prepared by each business and the Group's strategic plan. Beyond five years, cash flow projections utilise a perpetuity growth rate of 2%.

The key assumptions used to prepare the cash flow forecasts relate to gross margins, revenue growth rates and the discount rate. The gross margins are assumed to remain sustainable, which is supported by historical experience; revenue growth rates generally approximate to the average rates for the markets in which the business operates, unless there are particular factors relevant to a business, such as start-ups. The annual revenue growth rates used in the cash flow forecasts for the next five years represent the budgeted rates for 2018 and thereafter, average growth rates for each Sector; these annual growth rates then reduce to 2% over the longer term.

# 10. GOODWILL CONTINUED

The cash flow forecasts are discounted to determine a current valuation using a single market derived pre-tax discount rate of ca. 11% (2017: 12%). This single rate is based on the characteristics of lower risk, non-technically driven, distribution businesses operating generally in well developed markets and geographies and with robust capital structures. As these features are consistent between each of the Group's Sectors, the Board considers that it is more appropriate to use a single discount rate applied to each Sector's cash flow forecasts.

Based on the criteria set out above, no impairment in the value of goodwill in any of the Sectors was identified.

The Directors have also carried out sensitivity analysis on the key assumptions noted above to determine whether a "reasonably possible adverse change" in any of these assumptions would result in an impairment of goodwill. The analysis indicates that a "reasonably possible adverse change" would not give rise to an impairment charge to goodwill in any of the three Sectors.

# 11. ACQUISITION AND OTHER INTANGIBLE ASSETS

	Customer relationships £m	Supplier relationships £m	Trade names and databases £m	Total acquisition intangible assets £m	Other intangible assets £m
<b>Cost</b>					
At 1 October 2016	78.6	21.8	2.9	103.3	5.6
Additions	-	-	-	-	0.2
Acquisitions	2.3	7.8	-	10.1	-
Disposals	-	-	-	-	(0.1)
Exchange adjustments	(0.7)	-	(0.1)	(0.8)	(0.1)
At 30 September 2017	80.2	29.6	2.8	112.6	5.6
Additions	-	-	-	-	1.3
Acquisitions (note 22)	9.1	-	-	9.1	-
Disposals	-	-	-	-	(0.2)
Exchange adjustments	0.3	(0.1)	-	0.2	0.1
At 30 September 2018	89.6	29.5	2.8	121.9	6.8
<b>Amortisation</b>					
At 1 October 2016	33.3	12.9	2.5	48.7	4.6
Charge for the year	7.8	2.3	0.2	10.3	0.4
Disposals	-	-	-	-	(0.1)
Exchange adjustments	(0.4)	0.1	(0.1)	(0.4)	-
At 30 September 2017	40.7	15.3	2.6	58.6	4.9
Charge for the year	7.1	2.0	0.2	9.3	0.3
Disposals	-	-	-	-	(0.2)
Exchange adjustments	0.4	-	-	0.4	-
At 30 September 2018	48.2	17.3	2.8	68.3	5.0
<b>Net book value</b>					
At 30 September 2018	41.4	12.2	-	53.6	1.8
At 30 September 2017	39.5	14.3	0.2	54.0	0.7

Acquisition related charges are £9.6m (2017: £9.7m) and comprise £9.3m (2017: £10.3m) of amortisation of acquisition intangible assets, £0.5m of acquisition expenses (2017: £0.4m) and a credit of £0.2m relating to adjustments to deferred consideration (2017: £1.0m credit).

Acquisition intangible assets relate to items acquired through business combinations which are amortised over their useful economic life.

	Economic life
Customer relationships	5-15 years
Supplier relationships	8-10 years
Databases and trade names	5-10 years

Other intangible assets comprise computer software that is separately identifiable from IT equipment and includes software licences.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 30 SEPTEMBER 2018

### 12. INVESTMENT

	2018 £m	2017 £m
Investment	0.7	0.7

The Group holds a 10% interest in the share capital of Kunshan J Royal Precision Products Inc. ("JRPP"), a supplier to J Royal. The Group has no involvement in the day-to-day operations or management of JRPP. At 30 September 2018, there was no material difference between the book value of this investment and its fair value.

### 13. PROPERTY, PLANT AND EQUIPMENT

	Freehold properties £m	Leasehold properties £m	Plant and equipment £m	Hospital field equipment £m	Total £m
<b>Cost</b>					
At 1 October 2016	15.0	3.6	19.3	9.4	47.3
Additions	0.2	0.1	1.2	1.6	3.1
Acquisitions of businesses	–	–	0.2	0.8	1.0
Disposals	(0.5)	–	(0.8)	(0.5)	(1.8)
Exchange adjustments	(0.2)	0.1	1.2	0.2	1.3
At 30 September 2017	14.5	3.8	21.1	11.5	50.9
Additions	1.0	0.8	1.2	2.3	5.3
Acquisitions of businesses (note 22)	–	–	–	–	–
Disposals <sup>1</sup>	–	(0.3)	(2.3)	(0.7)	(3.3)
Exchange adjustments	0.4	(0.2)	0.4	(0.2)	0.4
At 30 September 2018	15.9	4.1	20.4	12.9	53.3
<b>Depreciation</b>					
At 1 October 2016	3.9	1.5	12.7	5.5	23.6
Charge for the year	0.5	0.4	1.8	1.6	4.3
Disposals	–	–	(0.8)	(0.4)	(1.2)
Exchange adjustments	–	0.1	1.3	0.2	1.6
At 30 September 2017	4.4	2.0	15.0	6.9	28.3
Charge for the year	0.5	0.4	1.8	1.8	4.5
Disposals <sup>1</sup>	–	(0.2)	(2.2)	(0.4)	(2.8)
Exchange adjustments	0.3	(0.2)	0.3	(0.1)	0.3
At 30 September 2018	5.2	2.0	14.9	8.2	30.3
<b>Net book value</b>					
At 30 September 2018	10.7	2.1	5.5	4.7	23.0
At 30 September 2017	10.1	1.8	6.1	4.6	22.6

<sup>1</sup> Includes £0.3m at net book value relating to the disposal of Bulldog (note 22).

Land included within freehold properties above, but which is not depreciated, is £3.4m (2017: £3.4m). Capital commitments contracted, but not provided, were £0.7m (2017: £1.1m) relating to the extension of the facility at IS-Sommer.

Freehold properties includes ca. 150 acres of land at Stamford ("the Stamford land") that comprises mostly farm land and former quarry land. In the Directors' opinion the current value of this land at 30 September 2018 is £1.0m (2017: £1.0m), with a book value of £Nil.

**14. DEFERRED TAX**

The movement on deferred tax is as follows:

	2018 £m	2017 £m
At 1 October	(8.2)	(7.4)
Credit for the year (note 7)	1.6	2.0
Acquisitions (note 22)	(1.6)	(2.0)
Accounted for in Other Comprehensive Income	(0.2)	(1.0)
Exchange adjustments	-	0.2
<b>At 30 September</b>	<b>(8.4)</b>	<b>(8.2)</b>

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances on a net basis.

	Assets		Liabilities		Net	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
Property, plant and equipment	0.6	0.5	(1.4)	(1.7)	(0.8)	(1.2)
Goodwill and intangible assets	-	-	(11.7)	(12.3)	(11.7)	(12.3)
Retirement benefit obligations	2.0	1.8	-	-	2.0	1.8
Inventories	1.5	1.8	(0.1)	(0.1)	1.4	1.7
Share-based payments	0.2	0.2	-	-	0.2	0.2
Trading losses	0.1	0.1	-	-	0.1	0.1
Other temporary differences	0.9	1.6	(0.5)	(0.1)	0.4	1.5
	5.3	6.0	(13.7)	(14.2)	(8.4)	(8.2)
Deferred tax offset	(5.0)	(5.8)	5.0	5.8	-	-
	0.3	0.2	(8.7)	(8.4)	(8.4)	(8.2)

No deferred tax has been provided on unremitted earnings of overseas Group companies as the Group controls the dividend policies of its subsidiaries. Unremitted earnings may be liable to overseas withholding tax (after allowing for double taxation relief) if they were to be distributed as dividends. The aggregate amount for which deferred tax has not been recognised in respect of unremitted earnings from overseas businesses of £122.1m was £6.3m (2017: £5.5m).

**15. INVENTORIES**

	2018 £m	2017 £m
Finished goods	82.9	73.2

Inventories are stated net of impairment provisions of £8.7m (2017: £8.3m). During the year £1.5m (2017: £1.3m) was recognised as a charge against operating profit, comprising the write-down of inventories to net realisable value.

**16. TRADE AND OTHER RECEIVABLES**

	2018 £m	2017 £m
Trade receivables	71.5	64.2
Less: impairment provision	(0.7)	(0.8)
	70.8	63.4
Other receivables	3.5	2.3
Prepayments and accrued income	3.3	3.2
	77.6	68.9

The maximum exposure to credit risk for trade receivables at 30 September, by currency, was:

	2018 £m	2017 £m
UK sterling	23.8	20.4
US dollars	16.0	13.9
Canadian dollars	10.2	10.2
Euro	12.3	10.3
Other	9.2	9.4
	71.5	64.2

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### 16. TRADE AND OTHER RECEIVABLES CONTINUED

Trade receivables, before impairment provisions, are analysed as follows:

	2018 £m	2017 £m
Not past due	59.2	52.3
Past due, but not impaired	11.6	11.1
Past due, but impaired	0.7	0.8
	<b>71.5</b>	<b>64.2</b>

The ageing of trade receivables classified as past due, but not impaired, is as follows:

	2018 £m	2017 £m
Up to one month past due	9.8	9.2
Between one and two months past due	1.4	1.4
Between two and four months past due	0.4	0.5
Over four months past due	-	-
	<b>11.6</b>	<b>11.1</b>

The movement in the provision for impairment of trade receivables is as follows:

	2018 £m	2017 £m
At 1 October	0.8	0.7
Charged against profit, net	(0.1)	0.1
Set up on acquisition	-	-
Utilised by write-off	-	-
<b>At 30 September</b>	<b>0.7</b>	<b>0.8</b>

#### 17. TRADE AND OTHER PAYABLES

	2018 £m	2017 £m
Trade payables	48.3	42.5
Other payables	3.6	3.3
Other taxes and social security	4.9	4.6
Accruals and deferred income	23.7	19.3
	<b>80.5</b>	<b>69.7</b>

The maximum exposure to foreign currency risk for trade payables at 30 September, by currency, was:

	2018 £m	2017 £m
UK sterling	11.2	10.7
US dollars	20.2	18.0
Canadian dollars	0.9	0.6
Euro	13.2	10.8
Other	2.8	2.4
	<b>48.3</b>	<b>42.5</b>

#### 18. CASH AND CASH EQUIVALENTS

	UK £m	US\$ £m	C\$ £m	Euro £m	Other £m	2018 Total £m	UK £m	US\$ £m	C\$ £m	Euro £m	Other £m	2017 Total £m
Cash at bank	4.7	4.3	1.1	2.9	1.6	14.6	6.0	4.1	2.3	3.2	2.7	18.3
Short term deposits	16.0	4.1	1.0	-	0.3	21.4	3.0	0.2	0.5	-	0.3	4.0
	<b>20.7</b>	<b>8.4</b>	<b>2.1</b>	<b>2.9</b>	<b>1.9</b>	<b>36.0</b>	<b>9.0</b>	<b>4.3</b>	<b>2.8</b>	<b>3.2</b>	<b>3.0</b>	<b>22.3</b>

The short term deposits and cash at bank are both interest bearing at rates linked to the UK base rate, or equivalent rate.



## 19. FINANCIAL INSTRUMENTS

The Group's overall management of the financial risks is carried out by a central treasury team under policies and procedures which are reviewed and approved by the Board. The treasury team identifies, evaluates and where appropriate, hedges financial risks in close cooperation with the Group's operating businesses. The treasury team does not undertake speculative foreign exchange dealings for which there is no underlying exposure.

The Group's principal financial instruments, other than a number of forward foreign currency contracts, comprise cash and short term deposits, investments, trade and other receivables and trade and other payables, borrowings and other liabilities. Trade and other receivables and trade and other payables arise directly from the Group's day-to-day operations.

The financial risks to which the Group is exposed are those of credit, liquidity, foreign currency, interest rate and capital management. An explanation of each of these risks, how the Group manages these risks and an analysis of sensitivities is set out below and on page 33 within Internal Control and Risk Management, all of which have been audited.

### a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations; this arises principally from the Group's trade and other receivables from customers and from cash balances (including deposits) held with financial institutions.

The Group is exposed to customers ranging from government backed agencies and large public and private wholesalers, to small privately owned businesses and the underlying local economic risks vary throughout the world. Trade receivable exposures are managed locally in the operating units where they arise and credit limits are set as deemed appropriate for each customer.

The Group establishes a provision for impairment that represents its estimate of potential losses in respect of specific trade and other receivables where it is deemed that a receivable may not be recoverable. When the receivable is deemed irrecoverable, the provision is written off against the underlying receivable. During the year, the Group had no significant unrecoverable trade receivables; there have been no other significant trade receivables written off in the past five years other than £0.2m written off in 2015.

Exposure to counterparty credit risk with financial institutions is controlled by the Group treasury team which establishes and monitors counterparty limits. Centrally managed funds are invested entirely with counterparties whose credit rating is "AA" or better.

The Group's maximum exposure to credit risk was as follows:

	Carrying amount	
	2018 £m	2017 £m
Trade receivables	70.8	63.4
Other receivables	3.5	2.3
Cash and cash equivalents	36.0	22.3
	110.3	88.0

There is no material difference between the book value of the financial assets and their fair value at each reporting date. An analysis of the ageing and currency of trade receivables and the associated provision for impairment is set out in note 16. An analysis of cash and cash equivalents is set out in note 18.

### b) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group continually monitors net cash and forecasts cash flows to ensure that sufficient resources are available to meet the Group's requirements in the short, medium and long term. Additionally, compliance with debt covenants are monitored regularly and during 2018 all covenants were complied with fully.

The Group is highly cash generative and uses monthly cash flow forecasts to monitor cash requirements and to optimise its return on shorter term deposits. Typically the Group ensures that it has sufficient cash on hand to meet foreseeable operational expenses, but the Group also maintains a committed revolving bank facility. This facility, which expires on 1 June 2020, is a committed three year multi-currency revolving facility for £30.0m with an accordion option to increase the committed facility by a further £30.0m up to a maximum of £60.0m and to extend the term up to five years. Interest on this facility is payable at between 70 and 115bps over LIBOR, depending on the ratio of net debt to EBITDA. None of the facility had been drawn down at 30 September 2018 (2017: £Nil).

The undrawn committed facilities available at 30 September are as follows:

	2018 £m	2017 £m
Expiring within one year	-	-
Expiring after two years	30.0	30.0

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### 19. FINANCIAL INSTRUMENTS CONTINUED

The Group's financial liabilities are as follows:

	Carrying amount	
	2018 £m	2017 £m
Trade payables	48.3	42.5
Other payables	3.6	3.3
Other liabilities (note 20)	5.6	6.6
	<b>57.5</b>	<b>52.4</b>
The maturities of the undiscounted financial liabilities are as follows:		
Less than one year	57.5	48.3
One to two years	-	4.5
Two to five years	-	-
	<b>57.5</b>	<b>52.8</b>
Less: discount	-	(0.4)
	<b>57.5</b>	<b>52.4</b>

There is no material difference between the book value of these financial liabilities and their fair value at each reporting date.

#### c) Currency risk

The Group's principal currency risk comprises translational and transactional risk from its exposure to movements in US dollars, Canadian dollars and Euros. The transactional exposure arises on trade receivables, trade payables and cash and cash equivalents and these balances are analysed by currency in notes 16, 17 and 18, respectively. Net foreign exchange gains of £0.1m (2017: £0.5m) were recognised in operating profit for the year.

The Group holds forward foreign exchange contracts in certain of the Group's businesses to hedge forecast transactional exposure to movements primarily in the US dollar and Euro. These forward foreign exchange contracts are classified as cash flow hedges and are stated at fair value. The notional value of forward contracts as at 30 September 2018 was £39.7m (2017: £33.0m). The net fair value of forward foreign exchange contracts used as hedges at 30 September 2018 was a £0.7m asset (2017: £0.9m liability). The amount removed from Other Comprehensive Income and taken to the Consolidated Income Statement in cost of sales during the year was a £0.9m credit (2017: £0.2m debit). The change in the fair value of cash flow hedges taken to Other Comprehensive Income during the year was a £0.7m credit (2017: £1.0m debit).

Management considers that the most significant foreign exchange risk relates to the US dollar, Canadian dollar and Euro. The Group's sensitivity to a 10% strengthening in UK sterling against each of these currencies (with all other variables held constant) is as follows:

	2018 £m
Decrease in adjusted operating profit (at average rates)	
US dollar: UK sterling	2.4
Canadian dollar: UK sterling	1.7
Euro: UK sterling	1.0
Decrease in total equity (at spot rates)	
US dollar: UK sterling	2.2
Canadian dollar: UK sterling	5.4
Euro: UK sterling	2.3

#### d) Interest rate risk

Interest rate risk is the risk that changes in interest rates will affect the Group's results. The Group's interest rate risk arises primarily from its cash funds and borrowings. The Group does not undertake any hedging of interest rates. All cash deposits, held in the UK and overseas, are held on a short term basis at floating rates or overnight rates, based on the relevant UK base rate, or equivalent rate. Surplus funds are deposited with commercial banks that meet the credit criteria approved by the Board, for periods of between one and six months at rates that are generally fixed by reference to the relevant UK base rate, or equivalent rate. An increase of 1% in interest rates would not have a significant impact on the Group's profit before tax. An analysis of cash and cash equivalents at the reporting dates is set out in note 18.

## 19. FINANCIAL INSTRUMENTS CONTINUED

### e) Fair values

There are no material differences between the book value of financial assets and liabilities and their fair value. The basis for determining fair values are as follows:

#### Derivatives

Forward exchange contracts are designated as level 1 assets (in the "fair value hierarchy") and valued at year end forward rates, adjusted for the forward points to the contract's value date with gains and losses taken to equity. No contract's maturity date is greater than 18 months from the year end.

#### Trade and other receivables/payables

As the majority of receivables/payables have a remaining life of less than one year, the book value is deemed to reflect the fair value.

#### Other liabilities

The carrying amount represents a discounted value of the expected liability which is deemed to reflect the fair value.

### f) Capital management risk

The Group's capital structure comprises cash funds and medium term bank borrowing facilities. The Group's objective when managing capital is to safeguard its ability to continue as a going concern and to maintain robust capital ratios to support the development of the business and provide strong returns to shareholders.

In order to maintain or adjust the capital structure, the Group may change the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or increase bank borrowings.

## 20. OTHER LIABILITIES

	2018 £m	2017 £m
Future purchases of minority interests	4.5	6.1
Deferred consideration	1.1	0.5
	5.6	6.6
Analysed as:		
Due within one year	5.6	2.5
Due after one year	-	4.1
The movement in the liability for future purchases of minority interests is as follows:		
	2018 £m	2017 £m
At 1 October	6.1	5.1
Acquisition of minority interest on exercise of options	(2.0)	-
Unwinding of discount	0.2	0.5
Fair value remeasurements	0.2	0.5
At 30 September	4.5	6.1

At 30 September 2018, the Group retained put options to acquire minority interests in Kentek and M Seals.

On 17 November 2017 and 30 March 2018, the Group completed the acquisition of the outstanding 10% minority interest in TPD for cash consideration of £2.0m (€2.3m). At 30 September 2018, the Group retained put options to acquire minority interests of 10% held in each of M Seals and Kentek which are both exercisable from November 2018.

At 30 September 2018, the estimate of the financial liability to acquire the outstanding minority shareholdings was reassessed by the Directors, based on their current estimate of the future performance of these businesses and to reflect foreign exchange rates at 30 September 2018. This led to a remeasurement of the fair value of these put options and the liability was increased by £0.2m (2017: £0.5m) reflecting a revised estimate of the future performance of the businesses and by a further £0.2m (2017: £0.5m) charge which arises from unwinding the discount on the liability. In aggregate £0.4m (2017: £1.0m) has been charged to the Consolidated Income Statement.

Deferred consideration comprises the following:

	2018 £m	2017 £m
Ascome	-	0.1
Edco	-	0.4
Coast	0.1	-
FS Cables	1.0	-
At 30 September	1.1	0.5

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### 20. OTHER LIABILITIES CONTINUED

The amounts outstanding at 30 September 2018 are expected to be paid within the next 12 months and will largely be based on the performance of these businesses in the period following their acquisition by the Group.

During the year, outstanding deferred consideration of £0.2m was paid to the vendors of Edco in respect of the performance of the business in the year ended 30 April 2018 and £0.1m was paid to the vendor of Ascome. A further £0.2m has been released to the Consolidated Income Statement as part of acquisition related charges in note 11.

#### 21. MINORITY INTERESTS

	£m
At 1 October 2017	4.3
Share of profit	0.7
Dividends paid	(0.2)
At 30 September 2017	4.8
Minority interest contribution	0.3
Share of minority net assets acquired of TPD	(2.5)
Share of profit	0.6
Dividends paid	(0.2)
Exchange adjustments	0.1
<b>At 30 September 2018</b>	<b>3.1</b>

External shareholders, represented by management in each business hold a 10% minority interest in M Seals and Kentek.

#### 22. ACQUISITION AND DISPOSAL OF BUSINESSES

On 16 October 2017, the Group acquired the trade and net assets of Coast Fabrications Inc. ("Coast"), based in California, US, for total cash consideration of £1.2m (US\$1.5m), which included £0.1m of acquisition expenses. The Company now trades as Clarendon Specialty Fasteners Inc.

On 21 August 2018, the Group acquired 100% of Caplink Limited and FSC Global Limited (collectively "FS Cables") based in St. Albans, UK, for the initial consideration of £24.3m, which included £7.3m of surplus cash and was before acquisition expenses of £0.4m. Maximum deferred consideration of £1.0m is payable based on the performance of FS Cables for the 12 months ended 31 October 2018.

Set out below is an analysis of the net book values and fair values relating to these acquisitions:

	FS Cables		Coast		Total	
	Book value £m	Fair value £m	Book value £m	Fair value £m	Book value £m	Fair value £m
Acquisition intangible assets	-	8.6	-	0.5	-	9.1
Deferred tax	-	(1.6)	-	-	-	(1.6)
Property, plant and equipment	0.3	-	-	-	0.3	-
Inventories	3.8	3.3	0.5	0.5	4.3	3.8
Trade and other receivables	2.5	2.5	0.3	0.3	2.8	2.8
Trade and other payables	(0.4)	(0.8)	(0.3)	(0.3)	(0.7)	(1.1)
Net assets acquired	6.2	12.0	0.5	1.0	6.7	13.0
Goodwill	-	5.5	-	0.2	-	5.7
	<b>6.2</b>	<b>17.5</b>	<b>0.5</b>	<b>1.2</b>	<b>6.7</b>	<b>18.7</b>
Cash paid		24.3		1.1		25.4
Cash acquired		(7.8)		-		(7.8)
Expenses of acquisition		0.4		0.1		0.5
<b>Net cash paid, after acquisition expenses</b>		<b>16.9</b>		<b>1.2</b>		<b>18.1</b>
Deferred consideration payable (note 20)		1.0		0.1		1.1
Less: expenses of acquisition		(0.4)		(0.1)		(0.5)
<b>Total consideration</b>		<b>17.5</b>		<b>1.2</b>		<b>18.7</b>

The fair values set out above are provisional and will be finalised in the next financial year. Goodwill of £5.7m recognised on these acquisitions represents the amount paid for future sales growth from both new customers and new products, operating cost synergies and employee know-how.

From the date of acquisition to 30 September 2018, the newly acquired Coast business contributed £4.0m to revenue and £0.2m to operating profit, the newly acquired FS Cables business contributed £1.1m to revenue and £0.2m to operating profit. If these businesses had been acquired at the beginning of the financial year, they would in aggregate have contributed on a pro-rata basis £17.6m to revenue and £2.8m to operating profit. However these amounts should not be viewed as indicative of the results of these businesses that would have occurred, if these acquisitions had been completed at the beginning of the year.

**22. ACQUISITION AND DISPOSAL OF BUSINESSES CONTINUED**

On 30 June 2018, Hercules Fluid Power Group, based in the US, sold the Bulldog Hydraulics and Gaskets business and trading assets at net asset value for net cash consideration of £4.0m (US\$5.4m), comprising tangible assets of £0.3m and net working capital of £3.7m. The business contributed revenues of £4.7m and an operating loss of £0.3m for the nine months ended 30 June 2018.

**23. RECONCILIATION OF OPERATING PROFIT TO CASH FLOW FROM OPERATING ACTIVITIES**

	2018 £m	2018 £m	2017 £m	2017 £m
<b>Operating profit</b>		<b>73.2</b>		68.5
Acquisition related charges (note 11)		<b>9.6</b>		9.7
CEO transition costs (note 28)		<b>2.1</b>		-
<b>Adjusted operating profit</b>		<b>84.9</b>		78.2
CEO transition costs paid (note 28)		<b>(0.8)</b>		-
		<b>84.1</b>		78.2
Depreciation or amortisation of tangible and other intangible assets	4.8		4.7	
Share-based payments expense (note 5)	1.0		0.8	
Defined benefit scheme expense (note 25)	(0.5)		(0.4)	
<b>Non-cash items</b>		<b>5.3</b>		5.1
<b>Operating cash flow before changes in working capital</b>		<b>89.4</b>		83.3
Increase in inventories	(8.3)		(5.1)	
Increase in trade and other receivables	(5.2)		(6.6)	
Increase in trade and other payables	8.4		7.7	
<b>Increase in working capital</b>		<b>(5.1)</b>		(4.0)
<b>Cash flow from operating activities, before acquisition expenses</b>		<b>84.3</b>		79.3

**24. CASH FUNDS**

The movement in cash during the year is as follows:

	2018 £m	2017 £m
Net increase in cash and cash equivalents	<b>13.1</b>	1.9
Decrease in borrowings	-	10.0
	<b>13.1</b>	11.9
Effect of exchange rates	<b>0.6</b>	(0.2)
<b>Movement in net cash</b>	<b>13.7</b>	11.7
Net cash at beginning of year	<b>22.3</b>	10.6
<b>Cash funds at end of year</b>	<b>36.0</b>	22.3
<b>Comprising:</b>		
Cash and cash equivalents	<b>36.0</b>	22.3
Borrowings	-	-
<b>Cash funds at 30 September</b>	<b>36.0</b>	22.3

The Group has a committed three year multi-currency revolving facility of £30.0m which expires on 1 June 2020 with an accordion option to increase the committed facility by a further £30.0m up to a maximum of £60.0m and a further option to extend the term up to five years. At 30 September 2018, the Group has utilised none of this facility (2017: ENil). Interest on this facility is payable between 70 and 115bps over LIBOR, depending on the ratio of net debt to EBITDA.

**25. RETIREMENT BENEFIT OBLIGATIONS**

The Group maintains two pension arrangements which are accounted for under IAS19 (Revised) "Employee Benefits". The principal arrangement is the defined benefit pension scheme in the UK, maintained by Diploma Holdings PLC and called the Diploma Holdings PLC UK Pension Scheme ("the Scheme"). This Scheme provides benefits based on final salary and length of service on retirement, leaving service or death and has been closed to further accrual since 5 April 2000.

The second and smaller pension arrangement is operated by Kubo in Switzerland and provides benefits on retirement, leaving service or death for the employees of Kubo in accordance with Swiss law. Kubo was acquired by the Group on 13 March 2015. The Kubo pension scheme is a defined contribution based scheme, which for technical reasons, is required under IFRS to be accounted for in accordance with IAS19 (revised).

The amount of pension deficit included in the Consolidated Statement of Financial Position in respect of these two pension arrangements is:

	2018 £m	2017 £m
Diploma Holdings PLC UK Pension Scheme	<b>6.8</b>	5.4
Kubo Pension Scheme	<b>3.7</b>	4.5
<b>Pension scheme net deficit</b>	<b>10.5</b>	9.9

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 30 SEPTEMBER 2018

## 25. RETIREMENT BENEFIT OBLIGATIONS CONTINUED

The amounts included in the Consolidated Income Statement in respect of these two pension arrangements are:

	2018 £m	2017 £m
Diploma Holdings PLC UK Pension Scheme	(0.1)	(0.3)
Kubo Pension Scheme	(0.2)	(0.2)
<b>Amounts charged to the Consolidated Income Statement</b>	<b>(0.3)</b>	<b>(0.5)</b>

Defined contribution schemes operated by the Group's businesses are not included in these disclosures.

**Diploma Holdings PLC UK Pension Scheme**

The Scheme is subject to a Statutory Funding Objective under the Pensions Act 2004 which requires that a valuation of the Scheme is carried out at least once every three years to determine whether the Statutory Funding Objective is met. As part of the process the Company must agree with the Trustees of the Scheme the contributions to be paid to address any shortfall against the Statutory Funding Objective. The most recent triennial actuarial valuation carried out as at 30 September 2016 reported that the Scheme had a funding deficit of £9.2m and held assets which covered 75% of its liabilities at that date. The next triennial actuarial valuation of the Scheme will be carried out as at 30 September 2019. There were no Scheme amendments, curtailments or settlements during the year.

On 28 September 2018 the Trustees completed a Buy-In of the pensioner liabilities in the Scheme with Just Retirement Limited. The Scheme paid £12.3m to Just Retirement Limited on 28 September 2018 to fund 95% of the Buy-In premium and £0.7m was paid on 22 October 2018 to fund the remaining 5% of the premium. The impact of this transaction has been reflected in the pension disclosures set out below.

The Scheme is managed by a set of Trustees appointed in part by the Company and in part from elections by members of the Scheme. The Trustees have responsibility for obtaining valuations of the fund, administering benefit payments and investing the Scheme's assets. The Trustees delegate some of these functions to their professional advisors where appropriate.

The Scheme exposes the Company and therefore the Group, to a number of risks:

- **Investment risk.** The Scheme holds investments in asset classes, such as equities, which have volatile market values and while these assets are expected to provide real returns over the long term, volatility over the short term can cause additional funding to be required if a deficit emerges.
- **Interest rate risk.** The Scheme's liabilities are assessed using market yields on high quality corporate bonds to discount the liabilities. As the Scheme's assets include equities, the value of the assets and liabilities may not move in the same way.
- **Inflation risk.** A significant proportion of the benefits under the Scheme are linked to inflation. The Scheme's assets are expected to provide a good hedge against inflation over the long term, however movements over the short term could lead to funding deficits emerging.
- **Mortality risk.** In the event that members live longer than assumed, a larger funding deficit may emerge in the Scheme.

**a) Pension deficit included in the Consolidated Statement of Financial Position**

	2018 £m	2017 £m
Market value of Scheme assets:		
Equities	20.0	24.8
Buy-In policy	9.5	-
Bonds	-	6.0
Cash	-	0.1
	<b>29.5</b>	<b>30.9</b>
Present value of Scheme liabilities	<b>(36.3)</b>	<b>(36.3)</b>
<b>Pension scheme net deficit</b>	<b>(6.8)</b>	<b>(5.4)</b>

The pension scheme net deficit includes £3.5m of historic annuities and related assets on a net basis, rather than on a gross basis.

**b) Amounts charged to the Consolidated Income Statement**

	2018 £m	2017 £m
Charged to operating profit	-	-
Interest cost on liabilities	(1.0)	(0.9)
Interest on assets	0.9	0.6
Charged to financial expense, net (note 6)	(0.1)	(0.3)
<b>Amounts charged to the Consolidated Income Statement</b>	<b>(0.1)</b>	<b>(0.3)</b>

## 25. RETIREMENT BENEFIT OBLIGATIONS CONTINUED

### c) Amounts recognised in the Consolidated Statement of Comprehensive Income

	2018 £m	2017 £m
Investment (loss)/gain on Scheme assets in excess of interest	(1.8)	2.7
Effect of changes in financial assumptions on Scheme liabilities	0.6	3.2
Effect of changes in demographic assumptions on Scheme liabilities	(0.6)	(1.3)
Experience adjustments on Scheme liabilities	-	(0.1)
<b>Actuarial (losses)/gains charged in the Consolidated Statement of Comprehensive Income</b>	<b>(1.8)</b>	<b>4.5</b>

The cumulative amount of actuarial losses recognised in the Consolidated Statement of Comprehensive Income, since the transition to IFRS, is £7.6m (2017: £5.8m).

### d) Analysis of movement in the pension deficit

	2018 £m	2017 £m
At 1 October	5.4	10.0
Amounts charged to the Consolidated Income Statement	0.1	0.3
Contributions paid by employer	(0.5)	(0.4)
Net effect of remeasurements of Scheme assets and liabilities	1.8	(4.5)
<b>At 30 September</b>	<b>6.8</b>	<b>5.4</b>

### e) Analysis of movements in the present value of the Scheme liabilities

	2018 £m	2017 £m
At 1 October	36.3	38.1
Interest cost on liabilities	1.0	0.9
Impact from changes in actuarial assumptions	-	(1.8)
Benefits paid	(1.0)	(0.9)
<b>At 30 September</b>	<b>36.3</b>	<b>36.3</b>

### f) Analysis of movements in the present value of the Scheme assets

	2018 £m	2017 £m
At 1 October	30.9	28.1
Interest on assets	0.9	0.6
Return on Scheme assets	(1.8)	2.7
Contributions paid by employer	0.5	0.4
Benefits paid	(1.0)	(0.9)
<b>At 30 September</b>	<b>29.5</b>	<b>30.9</b>

The actual return on the Scheme assets during the year was a £0.9m loss (2017: £3.3m gain).

#### Assets

The Scheme's assets are held in passive unit funds managed by Legal & General Investment Management and at 30 September 2018, the major categories of assets were as follows:

	2018 %	2017 %
North America equities	17	20
UK equities	17	20
European equities (non-UK)	17	20
Asia-Pacific and Emerging Markets equities	17	20
Buy-In policy	32	-
Corporate bonds	-	12
Index-linked gilts	-	8
Cash	-	-

### Principal actuarial assumptions for the Scheme at balance sheet dates

	2018 %	2017 %	2016 %	2015 %
Inflation rate – RPI	3.4	3.4	3.2	3.1
– CPI	2.4	2.4	2.4	2.3
Expected rate of pension increases – CPI	2.4	2.4	2.4	2.3
Discount rate	2.9	2.8	2.3	2.3

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

FOR THE YEAR ENDED 30 SEPTEMBER 2018

## 25. RETIREMENT BENEFIT OBLIGATIONS CONTINUED

## Demographic assumptions

Mortality table used:	S2NxA
Year the mortality table was published:	CMI 2017
Allowance for future improvements in longevity:	Year of birth projections, with a long term improvement rate of 1.0%
Allowance made for members to take a cash lump sum on retirement:	Members are assumed to take 100% of their maximum cash sum (based on current commutation factors)

The weighted average duration of the defined benefit obligation is around 18 years.

## Sensitivities

The sensitivities of the 2018 pension liabilities to changes in assumptions are as follows:

Factor	Assumption	Impact on pension liabilities	
		Estimated increase %	Estimated increase £m
Discount rate	Decrease by 0.5%	8.6	3.1
Inflation	Increase by 0.5%	3.7	1.3
Life expectancy	Increase by one year	2.7	1.0

## Risk mitigation strategies

When setting the investment strategy for the Scheme, the Trustees, in conjunction with the employer, take into account the liability profile of the Scheme. The current strategy is designed to broadly match assets and liabilities in respect of pensioner members, but to invest in growth assets in respect of deferred pensioners. Annuity policies have been taken out in respect of some historic pensioners, but the Scheme has not purchased annuities for retirements since 2005.

## Effect of the Scheme on the Group's future cash flows

The Company is required to agree a schedule of contributions with the Trustees of the Scheme following each triennial actuarial valuation. Following the triennial actuarial valuation carried out as at 30 September 2016, the Company agreed to contribute £0.5m in cash to the scheme annually. The next valuation of the Scheme will be carried out as at 30 September 2019.

## The Kubo Pension Scheme ("the Kubo Scheme")

In accordance with Swiss law, Kubo's pension benefits are contribution based with the level of benefits varying according to category of employment. Swiss law requires certain guarantees to be provided on such pension benefits. Kubo finances its Swiss pension benefits through the ASGA Pensionskasse, a multi-employer plan of non-associated companies which pools risks between participating companies. As at 30 September 2018 the ASGA Pensionskasse had a local coverage ratio of 110.7%.

Set out below is a summary of the key features of the Kubo Scheme.

## a) Pension deficit included in the Consolidated Statement of Financial Position

	2018 £m	2017 £m
Assets of the Kubo Scheme <sup>1</sup>	9.1	8.7
Actuarial liabilities of the Kubo Scheme	(12.8)	(13.2)
<b>Pension scheme net deficit</b>	<b>(3.7)</b>	<b>(4.5)</b>

<sup>1</sup> The assets of the Kubo Scheme are held as part of the funds managed by ASGA Pensionskasse.

## b) Amounts charged to the Consolidated Income Statement

	2018 £m	2017 £m
Service cost	(0.2)	(0.2)
<b>Amount charged to operating profit in the Consolidated Income Statement</b>	<b>(0.2)</b>	<b>(0.2)</b>

## c) Analysis of movement in the pension deficit

	2018 £m	2017 £m
At 1 October	4.5	7.2
Amounts charged to the Consolidated Income Statement	0.2	0.2
Contributions paid by employer	(0.2)	(0.2)
Net effect of remeasurements of Kubo Scheme assets and liabilities	(0.8)	(2.6)
Exchange adjustments	-	(0.1)
<b>At 30 September</b>	<b>3.7</b>	<b>4.5</b>



## 25. RETIREMENT BENEFIT OBLIGATIONS CONTINUED

### d) Amounts recognised in the Consolidated Statement of Comprehensive Income

The actuarial gain credited to the Consolidated Statement of Comprehensive Income is £0.8m (2017: £2.6m).

#### Principal actuarial assumptions for the Kubo Scheme at balance sheet dates

	2018	2017
Expected rate of pension increase	0%	0%
Expected rate of salary increase	1.0%	1.0%
Discount rate	1.0%	0.7%
Interest credit rate	1.0%	1.0%
Mortality	BVG2015	BVG2015

#### Sensitivities

The sensitivities of the 2018 pension liabilities to changes in assumptions are as follows:

Factor	Assumption	Impact on pension liabilities	
		Estimated increase %	Estimated increase £m
Discount rate	Decrease by 0.5%	10.6%	1.4
Life expectancy	Increase by one year	7.0%	0.9

#### Effect of the Kubo Scheme on the Group's future cash flows

	£m
Best estimate of employer's contribution in 2019	0.4
Best estimate of employees' contribution in 2019	0.3

The weighted average duration of the defined benefit obligation is approximately 20 years.

## 26. COMMITMENTS

At 30 September 2018 the Group had outstanding aggregate commitments for future lease payments (under non-cancellable operating leases) in respect of the following years:

	Land and buildings		Other		Total	
	2018 £m	2017 £m	2018 £m	2017 £m	2018 £m	2017 £m
Within one year	4.4	4.1	1.5	1.3	5.9	5.4
For years two to five	11.1	9.7	2.1	1.6	13.2	11.3
After five years	5.0	4.2	–	–	5.0	4.2
	20.5	18.0	3.6	2.9	24.1	20.9

Other commitments comprise plant and machinery, motor vehicles and office equipment. Operating lease payments made during the year in respect of land and buildings and other commitments were £4.6m (2017: £4.2m) and £1.6m (2017: £1.5m), respectively.

## 27. AUDITOR'S REMUNERATION

During the year the Group paid fees for the following services from the auditor:

	2018 £m	2017 £m
Fees payable to the auditor for the audit of:		
– the Company's Annual Report & Accounts	0.1	0.1
– the Company's subsidiaries	0.5	0.5
<b>Audit fees</b>	<b>0.6</b>	<b>0.6</b>

Non-audit fees of £15,000 (2017: £13,000) were paid to the Group's auditor for carrying out "agreed upon procedures" on the Half Year Announcement, which is unaudited.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS CONTINUED

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### 28. CHIEF EXECUTIVE OFFICER TRANSITION COSTS

Richard Ingram joined the Board on 23 April 2018 and was appointed Chief Executive Officer ("CEO") on 8 May 2018. Bruce Thompson retired as both CEO and Executive Director on 8 May 2018, but remained available to support an orderly transition until his retirement from the Company on 30 September 2018. Accordingly for a period of time during the year, the Company was bearing the costs of two CEO roles.

On 28 August 2018, Richard Ingram stepped down from his role as both CEO and as Executive Director and left the Company with immediate effect.

The one-off and incremental costs associated with the transition of the CEO comprise a significant restructuring cost to the Group and have been excluded in determining adjusted operating profit to present, the operational performance of the Group on a consistent basis. The costs relating to the CEO transition of £2.1m comprise:

	Charged in year £m	Paid in year £m	Outstanding at 30 September £m
Employment costs			
- as CEO	0.3	(0.3)	-
- in lieu of notice	0.5	(0.1)	0.4
Compensation on loss of office	0.4	-	0.4
Recruitment costs <sup>1</sup>	0.6	(0.3)	0.3
Other related costs, including advisors	0.3	(0.1)	0.2
	<b>2.1</b>	<b>(0.8)</b>	<b>1.3</b>

<sup>1</sup> Includes recruitment costs relating to new recruitment search project that commenced in August 2018.

#### 29. EXCHANGE RATES

The exchange rates used to translate the results of the overseas businesses are as follows:

	Average		Closing	
	2018	2017	2018	2017
US dollar (US\$)	1.35	1.27	1.30	1.34
Canadian dollar (C\$)	1.73	1.67	1.69	1.68
Euro (€)	1.13	1.15	1.12	1.13
Swiss franc (CHF)	1.31	1.26	1.27	1.30
Australian dollar (A\$)	1.78	1.67	1.80	1.71

#### 30. SUBSEQUENT EVENTS

On 12 October 2018, the Group completed the acquisition of Actios SAS, the parent company of the Gremtek Group ("Gremtek") of companies. Gremtek is a leading supplier of own-branded protective sleeving and cable identification products to a broad range of industrial markets, principally in France, but also in Germany and elsewhere in Europe. The initial consideration was £7.4m (£8.4m) with deferred consideration payable of up to £0.5m (£0.6m), based on performance in the year ending 31 December 2018. A review to determine fair values of the net assets acquired will be completed during the next financial year.

## GROUP ACCOUNTING POLICIES

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

The consolidated financial statements have been prepared in accordance with IFRS as endorsed by the EU and in accordance with the Companies Act 2006, as applicable to companies reporting under IFRS. The accounting policies set out below have been consistently applied in 2018 and the comparative year.

There were no new standards, amendments or interpretations to existing standards which have been published and endorsed by the EU and which have a significant impact on the results, financial position or presentation of the consolidated financial statements for the year ended 30 September 2018.

#### 1.1 BASIS OF PREPARATION

The consolidated financial statements have been prepared under the historical cost convention, except for derivative financial instruments which are held at fair value. The consolidated financial statements have been prepared on a going concern basis, as discussed on page 65.

#### 1.2 BASIS OF CONSOLIDATION

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control exists when the Company is exposed or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The assets, liabilities and results of subsidiaries acquired or disposed of 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 their accounting policies into line with those detailed herein to ensure that the Group financial statements are prepared on a consistent basis. All intra-Group transactions, balances, income and expenses are eliminated in preparing the consolidated financial statements.

Non-controlling interests, defined as minority interests, in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination.

#### 1.3 ACQUISITIONS

Acquisitions are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Goodwill at the acquisition date represents the cost of the business combination (excluding acquisition related costs, which are expensed as incurred) plus the amount of any non-controlling interest in the acquiree in excess of the fair value of the identifiable tangible and intangible assets, liabilities and contingent liabilities acquired.

Minority interests may be initially measured at fair value or, alternatively, at the minority interest's proportionate share of the recognised amounts of the acquiree's identifiable net assets. The choice of measurement basis is made for each business combination separately.

#### 1.4 DIVESTMENTS

The results and cash flows of major lines of businesses that have been divested have been classified as discontinued businesses. There were no discontinued operations in either 2018 or 2017.

#### 1.5 REVENUE RECOGNITION

Revenue is measured as the fair value of the consideration received or receivable for goods and services supplied to customers, after deducting sales allowances and value added taxes; revenue receivable for services supplied to customers, as opposed to goods, is less than ca. 3% of Group revenue. Revenue is recognised when the risk and rewards of ownership transfers to the customer, which depending on individual customer terms, is at the time of despatch, delivery or upon formal customer acceptance. Provision is made for returns where appropriate. Service revenue received in advance is deferred and recognised on a pro-rata basis over the period of the contract.

#### 1.6 EMPLOYEE BENEFITS

The Group operates a number of pension plans, both of the defined contribution and defined benefit type.

- a) Defined contribution pension plans: Contributions to the Group's defined contribution schemes are recognised as an employee benefit expense when they fall due.
- b) Defined benefit pension plan: The deficit recognised in the balance sheet for the Group's defined benefit pension plan is the present value of the defined benefit obligation at the balance sheet date less the fair value of the scheme assets. The defined benefit obligation is calculated by independent actuaries using the projected unit cost method and by discounting the estimated future cash flows using interest rates on high quality corporate bonds. The pension expense for the Group's defined benefit plan is recognised as follows:
  - i) Within the Consolidated Income Statement:
    - Gains and losses arising on settlements and curtailments - where the item that gave rise to the settlement or curtailment is recognised in operating profit.
    - Interest cost on the net deficit in the plan - calculated by applying the discount rate to the net defined benefit liability at the start of the annual reporting period.
  - ii) Within the Consolidated Statement of Comprehensive Income ("Other Comprehensive Income"):
    - Actuarial gains and losses arising on the assets and liabilities of the plan related to actual experience and any changes in assumptions at the end of the year.
- c) Share-based payments: Equity-settled transactions (which are where the Executive Directors and certain senior employees receive a part of their remuneration in the form of shares in the Company, or rights over shares) are measured at fair value at the date of grant. The fair value determined at the grant date takes account of the effect of market based measures, such as the Total Shareholder Return ("TSR") targets upon which vesting of part of the award is conditional and is expensed to the Consolidated Income Statement on a straight-line basis over the vesting period, with a corresponding credit to equity. The cumulative expense recognised is adjusted to take account of shares forfeited by Executives who leave during the performance or vesting period and, in the case of non-market related performance conditions, where it becomes unlikely that shares will vest. For the market-based measure, the Directors have used a predicted future value model to determine fair value of the shares at the date of grant.

The Group operates an Employee Benefit Trust for the granting of shares to Executives. The cost of shares in the Company purchased by the Employee Benefit Trust are shown as a deduction from equity.

## GROUP ACCOUNTING POLICIES CONTINUED

FOR THE YEAR ENDED 30 SEPTEMBER 2018

### 1.7 FOREIGN CURRENCIES

The individual financial statements of each Group entity are prepared in their functional currency, which is the currency of the primary economic environment in which that entity operates. For the purpose of the consolidated financial statements, the results and financial position of each entity are translated into UK sterling, which is the presentational currency of the Group.

- a) Reporting foreign currency transactions in functional currency: Transactions in currencies other than the entity's functional currency (foreign currencies) are initially recorded at the rates of exchange prevailing on the dates of the transactions. At each subsequent balance sheet date:
  - i) Foreign currency monetary items are retranslated at the rates prevailing at the balance sheet date. Exchange differences arising on the settlement or retranslation of monetary items are recognised in the Consolidated Income Statement.
  - ii) Non-monetary items measured at historical cost in a foreign currency are not retranslated.
  - iii) Non-monetary items measured at fair value in a foreign currency are retranslated using the exchange rates at the date the fair value was determined. Where a gain or loss on non-monetary items is recognised directly in equity, any exchange component of that gain or loss is also recognised directly in equity and conversely, where a gain or loss on a non-monetary item is recognised in the Consolidated Income Statement, any exchange component of that gain or loss is also recognised in the Consolidated Income Statement.
- b) Translation from functional currency to presentational currency: When the functional currency of a Group entity is different from the Group's presentational currency, its results and financial position are translated into the presentational currency as follows:
  - i) Assets and liabilities are translated using exchange rates prevailing at the balance sheet date.
  - ii) Income and expense items are translated at average exchange rates for the year, except where the use of such an average rate does not approximate the exchange rate at the date of the transaction, in which case the transaction rate is used.
  - iii) All resulting exchange differences are recognised in Other Comprehensive Income; these cumulative exchange differences are recognised in the Consolidated Income Statement in the period in which the foreign operation is disposed of.
- c) Net investment in foreign operations: Exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation are recognised in the Consolidated Income Statement in the separate financial statements of the reporting entity or the foreign operation as appropriate. In the consolidated financial statements such exchange differences are initially recognised in Other Comprehensive Income as a separate component of equity and subsequently recognised in the Consolidated Income Statement on disposal of the net investment.

### 1.8 TAXATION

The tax expense relates to the sum of current tax and deferred tax.

Current tax is based on taxable profit for the year, which differs from profit before taxation as reported in the Consolidated Income Statement. Taxable profit excludes items of income and expense that are taxable (or deductible) in other years and also excludes items that are never taxable or deductible. The Group's liability for current tax, including UK corporation tax and overseas tax, is calculated using rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method. Deferred tax is recognised 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. 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. Temporary differences arise primarily from the recognition of the deficit on the Group's defined benefit pension scheme, the difference between accelerated capital allowances and depreciation and for short term timing differences where a provision held against receivables or inventory is not deductible for taxation purposes. However, deferred tax 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 taxable profit, nor the accounting profit.

Deferred tax liabilities are also recognised for taxable temporary differences arising on investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is possible that the temporary difference will not reverse in the foreseeable future. No deferred tax is recognised on the unremitted earnings of overseas subsidiaries, as the Group controls the dividend policies of its subsidiaries.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled. Deferred tax is charged or credited to the Consolidated Income Statement, except when the item on which the tax or charge is credited or charged directly to equity, in which case the deferred tax is also dealt with in equity. 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 assets to be recovered. Tax assets and liabilities are offset when there is a legally enforceable right to enforce current tax assets against current tax liabilities and when the deferred income tax relates to the same fiscal authority.

### 1.9 PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Cost comprises the purchase price plus costs directly incurred in bringing the asset into use, but excluding interest. All repairs and maintenance expenditure is charged to the Consolidated Income Statement in the period in which it is incurred.

Freehold land is not depreciated. Depreciation on other items of property, plant and equipment begins when the asset is available for use and is charged to the Consolidated Income Statement on a straight-line basis to write off the cost, less residual value of the asset, over its estimated useful life as follows:

Freehold property	– between 20 and 50 years
Leasehold property	– term of the lease
Plant and equipment	– plant and machinery between 3 and 7 years
	– IT hardware between 3 and 5 years
	– fixtures and fittings between 5 and 15 years
Hospital field equipment	– 5 years

The depreciation method used, residual values and estimated useful lives are reviewed and changed, if appropriate, at least at each financial year end. 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. An asset's carrying amount is written down immediately to

its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses arising on disposals are determined by comparing sales proceeds with carrying amount and are recognised in the Consolidated Income Statement.

#### 1.10 INTANGIBLE ASSETS

All intangible assets, excluding goodwill arising on a business combination, are stated at their amortised cost or fair value at initial recognition less any provision for impairment.

##### a) Research and development costs

Research expenditure is written off as incurred. Development costs are written off as incurred unless forecast revenues for a particular project exceed attributable forecast development costs in which case they are capitalised and amortised on a straight-line basis over the asset's estimated useful life. Costs are capitalised as intangible assets unless physical assets, such as tooling, exist when they are classified as property, plant and equipment.

##### b) Computer software costs

Where computer software is not integral to an item of property, plant or equipment its costs are capitalised as other intangible assets. Amortisation is provided on a straight-line basis over its useful economic life of between three and seven years.

##### c) Acquired intangible assets – business combinations

Intangible assets that may be acquired as a result of a business combination, include, but are not limited to, customer lists, supplier lists, databases, technology and software and patents that can be separately measured at fair value, on a reliable basis, are separately recognised on acquisition at the fair value, together with the associated deferred tax liability. Amortisation is charged on a straight-line basis to the Consolidated Income Statement over the expected useful economic lives.

Fair values of customer and supplier relationships on larger acquisitions are valued using a discounted cash flow model; databases are valued using a replacement cost model. For smaller acquisitions, intangible assets are assessed using historical experience of similar transactions.

##### d) Goodwill – business combinations

Goodwill arising on the acquisition of a subsidiary represents the excess of the aggregate of the fair value of the consideration over the aggregate fair value of the identifiable intangible, tangible and current assets and net of the aggregate fair value of the liabilities (including contingent liabilities of businesses acquired at the date of acquisition). Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Transaction costs are expensed and are not included in the cost of acquisition.

#### 1.11 IMPAIRMENT OF TANGIBLE AND INTANGIBLE ASSETS

An impairment loss is recognised to the extent that the carrying amount of an asset or cash-generating unit ("CGU") exceeds its recoverable amount.

The recoverable amount of an asset or CGU is the higher of: (i) its fair value less costs to sell; and (ii) its value in use; its value in use is the present value of the future cash flows expected to be derived from the asset or CGU, discounted using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit. Impairment losses are recognised immediately in the Consolidated Income Statement.

##### a) Impairment of goodwill

Goodwill acquired in a business combination is allocated to a CGU; CGUs for this purpose are the Group's three Sectors which represent the lowest level within the Group at which the goodwill is monitored by the Group's Board of Directors for internal and

management purposes. CGUs to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired.

If the recoverable amount of the CGU is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the goodwill attributable to the CGU. Impairment losses cannot be subsequently reversed.

##### b) Impairment of other tangible and intangible assets

Other tangible and intangible assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Impairment losses and any subsequent reversals are recognised in the Consolidated Income Statement.

#### 1.12 INVENTORIES

Inventories are stated at the lower of cost (generally calculated on a FIFO and weighted average cost basis) and net realisable value, after making due allowance for any obsolete or slow moving inventory. Cost comprises direct materials, duty and freight-in costs.

Net realisable value represents the estimated selling price less all estimated costs of completion and the estimated costs necessary to make the sale.

#### 1.13 FINANCIAL INSTRUMENTS

Financial assets and liabilities are recognised in the Group balance sheet when the Group becomes a party to the contractual provisions of the instrument.

##### a) Trade receivables

Trade receivables are initially measured at fair value, do not carry any interest and are reduced by a charge for impairment for estimated irrecoverable amounts. Such impairment charges are recognised in the Consolidated Income Statement.

##### b) Trade payables

Trade payables are non-interest bearing and are initially measured at their nominal value.

##### c) Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, interest bearing deposits, bank overdrafts and short term highly liquid investments with original maturities of three months or less that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value. Bank overdrafts are repayable on demand and can form an integral part of the Group's cash management.

##### d) Put options held by minority interests

The purchase price of shares to be acquired under options held by minority shareholders in the Group's subsidiaries are calculated by reference to the estimated profitability of the relevant subsidiary at the time of exercise, using a multiple based formula. The net present value of the estimated future payments under these put options is shown as a financial liability. The corresponding entry is recognised in equity as a deduction against retained earnings. At the end of each year, the estimate of the financial liability is reassessed and any change in value is recognised in the Consolidated Income Statement, as part of finance income or expense. Where the liability is in a foreign currency, any change in the value of the liability resulting from changes in exchange rates is recognised in the Consolidated Income Statement.

##### e) Derivative financial instruments and hedge accounting

The Group holds derivative financial instruments in the form of forward foreign exchange contracts to hedge its foreign currency exposure. These derivatives are designated as cash flow hedges.

## GROUP ACCOUNTING POLICIES CONTINUED

FOR THE YEAR ENDED 30 SEPTEMBER 2018

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and subsequent changes in the fair value of foreign currency derivatives which are designated and effective as hedges of future cash flows are recognised in equity in the hedging reserve and in Other Comprehensive Income and are reclassified to profit or loss on maturity of the derivative. Changes in the fair value of foreign currency derivatives which are ineffective or do not meet the criteria for hedge accounting in accordance with IAS39 are recognised immediately in the Consolidated Income Statement.

The Group documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

No derivative contracts have been designated as fair value hedges or net investment hedges.

### f) Borrowings

Borrowings are initially recognised at the fair value of the consideration received. They are subsequently measured at amortised cost. Borrowings are classified as non-current when the repayment date is more than 12 months from the period end date or where they are drawn on a facility with more than 12 months to expiry.

### 1.14 INVESTMENTS (AVAILABLE FOR SALE FINANCIAL ASSETS)

The investment held by the Group comprises equity shares which are not held for the purposes of equity trading and in accordance with IAS39 is classified as available for sale. They are initially recognised at fair value. Subsequent to initial recognition, they are measured at fair value and changes therein are recognised in Other Comprehensive Income.

### 1.15 LEASES

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risk and rewards of ownership to the lessee. Leases include hire purchase contracts which have characteristics similar to finance or operating leases. All other leases are classified as operating leases. Rentals payable under operating leases are charged to the Consolidated Income Statement 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 expected lease term.

### 1.16 OTHER LIABILITIES

Other liabilities are recognised when the Group has legal or constructive obligation as a result of a past event and it is possible that the Group will be required to settle that obligation. Other liabilities are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date.

### 1.17 DIVIDENDS

The annual final dividend is not provided for until approved at the AGM; interim dividends are charged in the period they are paid.

### 1.18 SHARE CAPITAL AND RESERVES

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. The Group also maintains the following reserves:

- a) Translation reserve – The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign businesses.

- b) Hedging reserve – The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments that are determined to be an effective hedge.

- c) Retained earnings reserve – The retained earnings reserve comprises total cumulative recognised income and expense attributable to shareholders. Bonus issues of share capital and dividends to shareholders are also charged directly to this reserve. In addition the cost of acquiring shares in the Company and the liability to provide those shares to employees, is accounted for in this reserve.

Where any Group company purchases the Company's equity share capital and holds that share either directly as treasury shares or indirectly within an ESOP trust, the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to the Company's equity holders until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders. These shares are used to satisfy share awards granted to Directors under the Group's share schemes. The Trustee purchases the Company's shares on the open market using loans made by the Company or a subsidiary of the Company.

### 1.19 RELATED PARTIES

There are no related party transactions (other than with the key management) that are required to be disclosed in accordance with IAS24. Details of their remuneration are given in note 5 to the consolidated financial statements.

### 1.20 ACCOUNTING STANDARDS, INTERPRETATIONS AND AMENDMENTS TO PUBLISHED STANDARDS NOT YET EFFECTIVE

The IASB has published a number of new IFRSs ("standards"), amendments and interpretations to existing standards which are not yet effective, but will be mandatory for the Group's accounting periods beginning on or after 1 October 2018. An assessment of the impact of these new standards and interpretations is set out below:

#### IFRS15 Revenue from contracts with customers

IFRS15 replaces IAS18 and introduces a single, principles-based approach to recognition and measurement of revenue from sales contracts with customers. The new approach requires the identification of performance obligations in a sales contract and sets out when revenue is recognised based upon when those performance obligations have been met.

During 2018, a full analysis of the Group's significant revenue streams was undertaken with the assistance of key finance and management in each of the Group's businesses. The analysis performed enabled management to assess the impact of the new standard on the 2017 and 2018 financial statements.

This analysis confirmed that the majority of Group revenue is derived from the sale of products which generally have one performance obligation. Within the Life Sciences Sector there are a small number of contracts where goods and services are delivered and there is more than one performance obligation; in the majority of instances revenue for these contracts is already being separately recognised. Where revenue has been recognised for the delivery of goods, revenue recognition will be amended to ensure the element of revenue attributable to the service is separately recognised. The financial impact on revenues is not expected to be material.

The Group will adopt IFRS15 for the year commencing on 1 October 2018. As the anticipated impact of applying IFRS15 is not expected to be material, the Group will not restate the prior year consolidated financial statements.

#### **IFRS9 Financial Instruments**

IFRS9 replaces IAS39 and concerns the classification, measurement and de-recognition of financial assets and financial liabilities, introduces an expected credit loss model for the impairment of financial assets and sets out changes to the hedge accounting relationships.

During 2018, the Group completed an assessment of the impact of IFRS9 and concluded that adoption of this standard will not have a material impact on the Consolidated statement of Financial Position, as the categories of financial instruments are already being accounted for on the same measurement and valuation techniques as set out in IFRS9. The Group also determined that all existing hedge relationships will continue to qualify for hedge accounting under IFRS9.

An initial assessment of applying the expected credit loss model for the potential impairment of financial assets indicates that there is unlikely to be a material impact on the consolidated financial statements. The Group will adopt IFRS9 for the year commencing 1 October 2018. As the anticipated impact of adopting IFRS9 is not expected to be material, the Group will not restate the prior year financial statements on adoption.

#### **IFRS16 Leases**

IFRS16 replaces IAS17 and prescribes a single lessee accounting model that requires the recognition of an asset and a corresponding liability for all leases with terms over 12 months. The liability is measured at the present value of future lease payments for the lease term; depreciation of the assets and interest on the corresponding lease liabilities is recognised in the Income Statement over the lease term.

The Group anticipates that on implementation of IFRS16, there will be a material increase in the amount of the Group's lease liabilities, along with a corresponding increase in tangible property assets. The charge for operating leases in the Income Statement is unlikely to change materially, but the classification of this charge will change reflecting the new depreciation and interest cost respectively, in place of the existing lease cost. The Group's most significant operating leases relate to property as shown in note 26 to the consolidated financial statements.

The Group expects to adopt the modified retrospective approach with a cumulative adjustment to equity as at 1 October 2019 and as such will not restate the prior year financial statements. The Group will complete a full analysis of the likely impact of the standard during 2019 and will report this impact in next years' Annual Report & Accounts.

#### **1.21 ACCOUNTING ESTIMATES AND JUDGEMENTS**

The preparation of the Group's consolidated financial statements does not require management to make any critical accounting judgements, assumptions or estimates with regard to assets or liabilities that could potentially have a material adjustment to the carrying amount of assets or liabilities in the next 12 months.

Management however are required to make judgements, assumptions and estimates relating to certain assets and liabilities that could potentially have a material impact over the longer term. These relate to:

##### **1.21.1 ACQUISITION ACCOUNTING AND GOODWILL IMPAIRMENT**

When the Group makes an acquisition it recognises the identifiable assets and liabilities, including intangible assets, at fair value with the difference between the fair value of net assets acquired and the fair value of consideration paid comprising goodwill. Acquisitions are accounted for using the acquisition method as described in note 1.3 and 1.10 of The Group Accounting Policies. The key assumptions and estimates used to determine the valuation of intangible assets acquired are the forecast cash flows, the discount rate and customer/supplier attrition. Customer and supplier relationships are valued using a discounted cash flow model. Acquisitions often comprise an element of deferred consideration and may include a minority interest, which are subject to put options. These put options are valued at fair value at the date of acquisition. Deferred consideration is fair valued based on the Directors' estimate of future performance of the acquired entity.

The Group's growth strategy is underpinned by the successful execution of acquisitions. This results in material amounts of goodwill and intangible assets (principally customer and supplier relationships) being recognised in the Consolidated Statement of Financial Position. As set out in note 1.11 of The Group Accounting Policies, goodwill is tested annually to determine if there is any indication of impairment. Assumptions are then used to determine the recoverable amount of each CGU, principally based on the present value of estimated future cash flows to derive the "value in use" to the Group of the capitalised goodwill. The key estimates made and assumptions used in performing impairment testing this year are set out in note 10 to the consolidated financial statements.

##### **1.21.2 INVENTORY PROVISIONS**

Inventories are stated at the lower of cost and net realisable value as set out in note 1.12 of The Group Accounting Policies. In the course of normal trading activities, judgement is used to establish the net realisable value of inventory and impairment charges are made for obsolete or slow-moving inventories and against excess inventories.

The decision to make an impairment charge is based on a number of factors including management's assessment of the current trading environment, aged profiles and historical usage and other matters which are relevant at the time the consolidated financial statements are approved.

##### **1.21.3 DEFINED BENEFIT PENSION**

Defined benefit pensions are accounted for as set out in note 1.6 of The Group Accounting Policies. Determining the value of the future defined benefit obligation requires estimates in respect of the assumptions used to calculate present values. These include discount rate, future mortality and inflation rate. Management makes these estimates in consultation with an independent actuary. Details of the estimates and key sensitivities made in calculating the defined benefit obligation at 30 September 2018 are set out in note 25 to the consolidated financial statements.

## PARENT COMPANY STATEMENT OF FINANCIAL POSITION

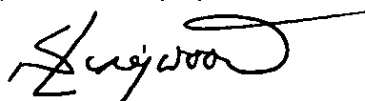
### AS AT 30 SEPTEMBER 2018

	Note	2018 £m	2017 £m
<b>Fixed assets</b>			
Investments	d	72.0	72.0
<b>Creditors: amounts falling due within one year</b>			
Amounts owed to subsidiary undertakings		(14.4)	(17.1)
<b>Net assets</b>		<b>57.6</b>	<b>54.9</b>
<b>Capital and reserves</b>			
Called up share capital	e	5.7	5.7
Profit and loss account <sup>1</sup>		51.9	49.2
<b>Total shareholders' equity</b>		<b>57.6</b>	<b>54.9</b>

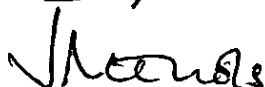
<sup>1</sup> Includes profit for the year of £4.1m (2017: £2.8m).

The financial statements of Diploma PLC, company number 3899848, were approved by the Board of Directors on 19 November 2018 and signed on its behalf by:

NP Lingwood  
Group Finance Director



JE Nicholas  
Chairman



## PARENT COMPANY STATEMENT OF CHANGES IN EQUITY

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

	Note	Share capital £m	Retained earnings £m	Total Shareholders' equity £m
At 1 October 2016		5.7	45.8	51.5
Total Comprehensive Income	a	–	26.2	26.2
Dividends paid		–	(23.5)	(23.5)
Settlement of LTIP awards	e	–	0.7	0.7
At 30 September 2017		5.7	49.2	54.9
Total Comprehensive Income	a	–	30.9	30.9
Dividends paid		–	(26.8)	(26.8)
Settlement of LTIP awards	e	–	(1.4)	(1.4)
<b>At 30 September 2018</b>		<b>5.7</b>	<b>51.9</b>	<b>57.6</b>



## NOTES TO THE PARENT COMPANY FINANCIAL STATEMENTS

### FOR THE YEAR ENDED 30 SEPTEMBER 2018

#### A) ACCOUNTING POLICIES

##### a.1) Basis of accounting

The Parent Company financial statements ("Financial Statements") have been prepared in accordance with the Companies Act 2006 and FRS101 "Reduced Disclosures Framework". The Directors confirm they have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future and accordingly, they continue to adopt the going concern basis in preparing the Financial Statements. The Financial Statements, which are prepared on a historical cost basis, are presented in UK sterling and all values are rounded to the nearest million pounds (£m) except when otherwise indicated.

The following disclosures have not been provided as permitted by FRS101:

- a cash flow statement and related notes;
- a comparative period reconciliation for share capital;
- disclosures in respect of transactions with wholly owned subsidiaries;
- disclosures in respect of capital management;
- the effects of new but not yet effective IFRS;
- disclosures in respect of the compensation of key management personnel as required.

The Company has also taken the exemption under FRS101 available in respect of the requirements of paragraphs 45(b) and 46 to 52 of IFRS2 "Share-based Payment" in respect of Group settled share-based payments as the consolidated financial statements of the Company include the equivalent disclosures.

##### a.2) Total Comprehensive Income

Total Comprehensive Income comprises dividends received from subsidiaries, interest payable on inter-company balances at the UK Base Rate, plus 1.5% and that are repayable on demand. Total Comprehensive Income is distributable to shareholders.

##### a.3) Dividends

Dividend income is recognised when received. Final dividend distributions are recognised in the Company's Financial Statements in the year in which the dividends are approved by the Company's shareholders. Interim dividends are recognised when paid.

The capacity of the Company to make dividend payments is primarily determined by the availability of retained distributable reserves and cash resources. As at 30 September 2018 the Company had distributable reserves of £51.9m (2017: £49.2m) and the total external dividends declared in 2018 amounted to £26.8m. When required the Company can receive dividends from its subsidiaries to further increase distributable reserves.

##### a.4) Diploma PLC Employment Benefit Trust and employee share schemes

Shares held by the Diploma PLC Employee Benefit Trust ("the Trust") are stated at cost and accounted for as a deduction from shareholders' equity in accordance with IAS32, as applied by FRS101. Shares that are held by the Trust are not eligible for dividends until such time as the awards have vested and options have been exercised by the participants.

##### a.5) Auditor's remuneration

Fees payable to the auditor for the audit of the Company's financial statements of £3,500 (2017: £3,500) were borne by a fellow Group undertaking.

#### B) DIRECTORS' AND EMPLOYEES' REMUNERATION

No remuneration is paid directly by the Company; information on the Directors' remuneration (which is paid by a subsidiary company) and their interests in the share capital of the Company are set out in the Remuneration Committee Report on pages 49 to 63. The Company had no employees (2017: none).

#### C) COMPANY PROFIT AND LOSS ACCOUNT

As permitted by section 408 of the Companies Act 2006, no separate profit and loss account is presented for the Company. There were no gains or losses either in the current or preceding years recognised in other comprehensive income. The movement in the Company's profit and loss account reserves include a profit for the year of £4.1m (2017: £2.8m), before settlement of LTIP awards.

#### D) INVESTMENTS

	£m
Shares in Group undertakings	
<b>At 30 September 2018 and 1 October 2017</b>	<b>72.0</b>

A full list of subsidiary and other related undertakings is set out on page 102.

#### E) CALLED UP SHARE CAPITAL

	2018 Number	2017 Number	2018 £m	2017 £m
Allotted, issued and fully paid ordinary shares of 5p each				
<b>At 30 September</b>	<b>113,239,555</b>	<b>113,239,555</b>	<b>5.7</b>	<b>5.7</b>

During the year 92,530 ordinary shares in the Company (2017: 79,679) were transferred from the Trust to participants on an after income tax basis in connection with the exercise of options in respect of awards which had vested under the 2011 Long Term Incentive Plan, as set out on pages 59 and 63 in the Remuneration Committee Report. The Trust also purchased 100,000 ordinary shares in the Company for £1.2m (2017: £Nil) during the year. At 30 September 2018, the Trust held 100,368 (2017: 92,898) ordinary shares in the Company representing 0.1% of the called up share capital. The market value of the shares at 30 September 2018 was £1.4m (2017: £1.0m).

## INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF DIPLOMA PLC

### REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

#### OPINION

In our opinion:

- Diploma PLC's Group financial statements and Parent Company financial statements (the "financial statements") give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 30 September 2018 and of the Group's profit and cash flows 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 (United Kingdom Accounting Standards, comprising FRS101 "Reduced Disclosure Framework", and applicable law); 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, included within the Annual Report & Accounts (the "Annual Report"), which comprise: the consolidated and Parent Company statements of financial position as at 30 September 2018; the consolidated income statement and consolidated statement of comprehensive income, the consolidated cash flow statement, and the consolidated and Parent Company statements of changes in equity for the year then ended; the accounting policies; and the notes to the financial statements.

Our opinion is consistent with our reporting to the Audit Committee.

#### BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### Independence

We remained independent of the Group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the Group or the Parent Company.

Other than those disclosed in note 27 to the financial statements, we have provided no non-audit services to the Group or the Parent Company in the period from 1 October 2017 to 30 September 2018.

#### OUR AUDIT APPROACH

##### Context

In this first year of our audit tenure, our planning procedures involved meetings with Group and local business management, and the Board, to understand the business, its challenges, opportunities and associated risks.

##### Overview



- Overall Group materiality: £3.6 million, based on 5% of profit before tax.
- Overall Parent Company materiality: £0.7 million, based on 1% of total assets.
- We conducted audit work over 23 reporting units across nine countries in which the Group has significant operations
- The reporting units where we performed an audit of their complete financial information accounted for 79% of Group revenue and 83% of Group profit before tax
- The Group engagement team performed the audit work on five of the reporting units and visited, in person, two component teams who were responsible for the audit of eight reporting units across two countries. The visits included attendance at audit clearance meetings and discussions on the audit approach and findings with those local teams
- For those countries not visited in person we attended their clearance meetings via conference call or video conference
- We maintained regular contact with the local teams and evaluated the outcome of their audit work
- Provisions for impairment of inventories (Group).
- Recoverability of goodwill and the impairment assessment (Group).

### The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the Directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

We gained an understanding of the legal and regulatory framework applicable to the Group and the industries in which it operates, and considered the risk of acts by the Group which were contrary to applicable laws and regulations, including fraud. We designed audit procedures at Group and significant component level to respond to the risk, recognising that the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. We focused on laws and regulations that could give rise to a material misstatement in the Group and Parent Company financial statements, including, but not limited to, the Companies Act 2006, the Listing Rules, UK tax legislation and equivalent local laws and regulations applicable to component teams. Our tests included, but were not limited to, review of the financial statement disclosures to underlying supporting documentation, enquiries of management, review of certain component auditors' work and review of internal audit reports in so far as they related to the financial statements. There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it.

We did not identify any key audit matters relating to irregularities, including fraud. As in all of our audits we also addressed the risk of management override of internal controls, including testing journals and evaluating whether there was evidence of bias by the Directors that represented a risk of material misstatement due to fraud.

### Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the 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) identified by the auditors, including 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, and any comments we make on the results of our procedures thereon, 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. This is not a complete list of all risks identified by our audit.

Key audit matter	How our audit addressed the key audit matter
<p><b>Provisions for impairment of inventories</b> Refer to page 45 (Financial reporting and significant financial judgements) and note 15 (Inventories).</p> <p>The Group holds significant levels of inventory with total inventory, at 30 September 2018, of £82.9m which is recorded net of a provision of £8.7m.</p> <p>There is a risk associated with the valuation of slow moving and excess stock for which each business within the Group provides. There are different inventory provision methodologies, specific to the individual business, across the Group. There is significant management judgement and estimation involved in assessing the accuracy of the provision based upon the ageing and expected demand for the inventory.</p> <p>Therefore, we have determined that there is a significant risk that the inventory provision is not appropriate and therefore that inventory is recorded above its net realisable value.</p>	<p>Our audit procedures included understanding and evaluating the controls and systems related to the inventory provision process, together with substantive audit procedures.</p> <p>The substantive audit procedures performed for each individual component varied, depending upon the component team and the nature of the businesses and the inventory provision methodology, including the following procedures:</p> <ul style="list-style-type: none"> <li>• We obtained management's inventory provision and checked the mathematical accuracy of the provision based upon the provision methodology in place for that component.</li> <li>• We tested where applicable and on a sample basis, the accuracy of the ageing and demand reports used.</li> <li>• We evaluated the appropriateness of each businesses inventory provision methodology and the key assumptions within the provision model based upon the nature of the business and its inventory and the historic accuracy of the provision compared to actual write-offs.</li> <li>• We compared the actual sales value of a sample of inventory items to their book value to confirm that the carrying value of inventory does not exceed its net realisable value.</li> </ul> <p>As the Group engagement team, we were specifically involved in reviewing and assessing the appropriateness of the audit approach for each component in this area. This satisfied us that sufficient focus was placed on the more judgemental areas and that, whilst complex, the area was well understood and sufficient focus was placed on the risk area.</p>

## INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF DIPLOMA PLC CONTINUED

### REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS CONTINUED

Key audit matter	How our audit addressed the key audit matter
<p><b>Risk of impairment of goodwill</b> Refer to page 45 (Financial reporting and significant financial judgements) and note 10 (Goodwill).</p> <p>The Group has goodwill of £128.5m as at 30 September 2018, the most significant asset on the statement of financial position, which is required to be tested for impairment on an annual basis. Management has allocated the goodwill to three individual cash-generating units ("CGUs"): Life Sciences, Seals and Controls.</p> <p>We focused on this area due to the size of the goodwill balance and the level of judgement and estimation around the determination of the recoverable amount, being the higher of value in use and fair value less costs of disposal. Recoverable amounts are based on management's view of the future results and prospects of the business, the appropriate discount rates to be applied and specific risk factors applied to the CGUs.</p> <p>The key judgements in determining the recoverable amount of these CGUs relate to the forecast cash flows, long-term growth rates and the discount factor applied.</p> <p>We did not consider there to be a significant risk associated with any of the individual CGUs due to the continued growth in the business in the year and the historic levels of headroom.</p>	<p>We evaluated the process by which management prepared its cash flow forecasts and compared them against the latest Board strategy paper. We evaluated the historical accuracy of the plans, for example by comparing the forecasts used in the prior year model to the actual performance in the current year. These procedures enabled us to determine the accuracy of the forecasting process and apply appropriate sensitivities to the cash flows.</p> <p>We obtained management's goodwill impairment review calculations and checked the mechanical accuracy of the model.</p> <p>We assessed the appropriateness of management's discount rates, future cash flows and long-term growth rates. We benchmarked assumptions against industry and peer group comparators and metrics such as country inflation rates.</p> <p>Based upon our assessments described above, we challenged management on the appropriateness of its calculations by applying our own sensitivity analysis to the forecast cash flows, long-term growth rates and discount rates to ascertain the extent to which reasonable changes would, either individually or in aggregate, require an impairment of the goodwill.</p> <p>We determined that no impairment charges were required, based on the results of our work.</p>

#### How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the Group and the Parent Company, the accounting processes and controls, and the industry in which they operate.

The Group is focused on three core sectors; Life Sciences, Seals and Controls with operations primarily geographically located in Canada, the USA, the UK and continental Europe. Within the aforementioned Sectors are a number of businesses/management reporting entities which are consolidated by Group management. The Group financial statements are a consolidation of multiple reporting units representing the operating businesses within these three core sectors.

The reporting units vary in size and we identified 23 reporting units across nine countries in which the Group has significant operations that required an audit of their complete financial information due to their individual size. The components where we performed an audit of their complete financial information accounted for 83% of the Group's profit before tax, and 79% of the Group's revenue. Included within these 23 reporting units were five components that were audited by the Group engagement team, including four UK Controls trading businesses and the company which holds the UK pension scheme.

The reporting units, excluding those audited by the Group team, are audited by nine component teams. The Group engagement team visited two of the nine component teams, who were responsible for the audit of eight reporting units, to meet with local management, attend audit clearance meetings and discuss the audit approach and audit findings. For those components not visited we attended their clearance meetings either via conference call or video conference.

Our attendance at the clearance meetings, review and discussion of the audit results at overseas locations, together with the additional procedures performed at a Group level, gave us the evidence we needed for our opinion on the Group financial statements as a whole. Our audit procedures at the Group level included the audit of the consolidation, the goodwill impairment review and certain tax procedures.

## Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

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>Overall materiality</b>	£3.6 million.	£0.7 million.
<b>How we determined it</b>	5% of profit before tax.	1% of total assets.
<b>Rationale for benchmark applied</b>	We consider PBT to be an appropriate measure for a listed group and one of the key measures used by the shareholders in assessing the performance of the Group.	We believe that total assets is the primary measure used by the shareholders in assessing the performance of a holding company and is a generally accepted auditing benchmark.

For each component in the scope of our Group audit, we allocated a materiality that is less than our overall Group materiality. The range of materiality allocated across components was between £3.2 million and £0.3 million. Certain components were audited to a local statutory audit materiality that was less than our allocated component materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £184,000 (Group audit) and £36,000 (Parent Company audit) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

## Going concern

In accordance with ISAs (UK) we report as follows:

Reporting obligation	Outcome
We are required to report if we have anything material to add or draw attention to in respect of the Directors' statement in the financial statements about whether the Directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the Directors' identification of any material uncertainties to the Group's and the Parent Company's ability to continue as a going concern over a period of at least 12 months from the date of approval of the financial statements.	We have nothing material to add or to draw attention to. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's and Parent Company's ability to continue as a going concern.
We are required to report if the Directors' statement relating to going concern in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.	We have nothing to report.

## REPORTING ON OTHER INFORMATION

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The Directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance 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 an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of 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. We have nothing to report based on these responsibilities.

With respect to the Strategic Report, Directors' Report and Corporate Governance Statement, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, the Companies Act 2006 (CA06), ISAs (UK) and the Listing Rules of the Financial Conduct Authority ("FCA") require us also to report certain opinions and matters as described below (required by ISAs (UK) unless otherwise stated).

## Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 30 September 2018 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the Group and Parent Company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report. (CA06)

## INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF DIPLOMA PLC CONTINUED

### REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS CONTINUED

#### Corporate Governance Statement

In our opinion, based on the work undertaken in the course of the audit, the information given in the Governance section (on page 46) about internal controls and risk management systems in relation to financial reporting processes and about share capital structures in compliance with rules 7.2.5 and 7.2.6 of the Disclosure Guidance and Transparency Rules sourcebook of the FCA ("DTR") is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06).

In light of the knowledge and understanding of the Group and Parent Company and their environment obtained in the course of the audit, we did not identify any material misstatements in this information. (CA06).

In our opinion, based on the work undertaken in the course of the audit, the information given in the Corporate Governance Statement (on pages 39 to 42) with respect to the Parent Company's corporate governance code and practices and about its administrative, management and supervisory bodies and their committees complies with rules 7.2.2, 7.2.3 and 7.2.7 of the DTR. (CA06).

We have nothing to report arising from our responsibility to report if a corporate governance statement has not been prepared by the Parent Company. (CA06).

#### The Directors' assessment of the prospects of the Group and of the principal risks that would threaten the solvency or liquidity of the Group

We have nothing material to add or draw attention to regarding:

- The Directors' confirmation on page 30 of the Annual Report 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.
- The disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.
- The Directors' explanation on page 30 of the Annual Report 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 have nothing to report having performed a review of the Directors' statement that they have carried out a robust assessment of the principal risks facing the Group and statement in relation to the longer-term viability of the Group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the Directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the UK Corporate Governance Code (the "Code"); and considering whether the statements are consistent with the knowledge and understanding of the Group and Parent Company and their environment obtained in the course of the audit. (Listing Rules)

#### Other Code provisions

We have nothing to report in respect of our responsibility to report when:

- The statement given by the Directors, on page 65, that they consider the Annual Report taken as a whole to be fair, balanced and understandable, and provides the information necessary for the members to assess the Group's and Parent Company's position and performance, business model and strategy is materially inconsistent with our knowledge of the Group and Parent Company obtained in the course of performing our audit.
- The section of the Annual Report on page 44 describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.
- The Directors' statement relating to the Parent Company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified, under the Listing Rules, for review by the auditors.

#### Directors' remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006. (CA06)

### RESPONSIBILITIES FOR THE FINANCIAL STATEMENTS AND THE AUDIT

#### Responsibilities of the Directors for the financial statements

As explained more fully in the Directors' Responsibility Statement set out on page 65, the Directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The Directors are also responsible for such internal control as they 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.

#### Auditors' 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 auditors' 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.

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 auditors' report.

#### Use of this report

This report, including the opinions, has been prepared for and only for the Parent Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

#### OTHER REQUIRED REPORTING

##### COMPANIES ACT 2006 EXCEPTION REPORTING

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
- certain disclosures of Directors' remuneration specified by law are not made; or
- the Parent Company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

#### APPOINTMENT

Following the recommendation of the Audit Committee, we were appointed by the members on 1 March 2018 to audit the financial statements for the year ended 30 September 2018 and subsequent financial periods. This is therefore our first year of uninterrupted engagement.



Christopher Burns (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London  
19 November 2018

## SUBSIDIARIES OF DIPLOMA PLC

	Registered Office address*		Registered Office address*
<b>Life Sciences</b>		<b>Abbeychart Limited<sup>1</sup></b>	A
Somagen Diagnostics Inc.	F	HA Wainwright Limited <sup>1</sup>	A
AMT Electrosurgery Inc.	V	Hawco Refrigeration Limited <sup>1</sup>	A
Vantage Endoscopy Inc.	V	Microtherm UK Limited <sup>1</sup>	A
Big Green Surgical Company Pty Limited	X	IS Group (Europe) Limited <sup>1</sup>	A
Diagnostic Solutions Pty Limited	X	Specialty Fasteners Limited <sup>1</sup>	A
Diploma Healthcare Group NZ Limited	Z	Specialty Fasteners & Components Limited <sup>1</sup>	A
Techno-Path (Distribution) Limited	J	FSC UK Limited <sup>1</sup>	A
Abacus dx Pty Limited	X	FS Cables limited <sup>1</sup>	A
Abacus dx Limited	Z	FSC Global Limited <sup>2</sup>	A
A1-CBISS Limited	A	Caplink Limited	A
a1-envirosciences GmbH	G		
a1-Envirosciences Limited <sup>1</sup>	A	<b>Intermediate holding companies</b>	
Hitek Limited <sup>1</sup>	A	Diploma Holdings PLC	A
Hitek Group Limited <sup>1</sup>	A	Diploma Holdings Inc.	C
		Pride Limited	A
<b>Seals</b>		Diploma Australia Holdings Limited	A
HB Sealing Products Inc.	D	Diploma Canada Holdings Limited	A
J Royal US, Inc.	C	Diploma Overseas Limited	A
HKX Inc.	E	Napier Group Limited	A
All Seals Inc.	B	Williamson, Cliff Limited	A
RTD Seals Corp.	C	Newlandglebe Limited	A
HB Sealing Products Limited	W	Diploma Germany Holding GmbH	H
M Seals A/S <sup>3</sup>	S	Diploma Canada Healthcare Inc	F
M Seals AB <sup>3</sup>	T	Diploma Australia Healthcare Pty Limited	X
M Seals UK Limited <sup>2</sup> (formerly, M Seals NCL Limited)	A	Diploma Australia Seals Pty Limited	X
EDCO Seal and Supply Limited <sup>2</sup>	A		
Diploma (Tianjin) Trading Co. Limited	AB		
FPE Seals Limited	A		
A.B. Seals Limited <sup>1</sup>	A		
Swan Seals (Aberdeen) Limited <sup>1</sup>	A		
FPE Seals BV	P		
Kentek Oy <sup>3</sup>	K		
ZAO Kentek <sup>3</sup>	O		
Kentek Eesti Ou <sup>3</sup>	L		
SIA Kentek Latvija <sup>3</sup>	M		
UAB Kentek Lietuva <sup>3</sup>	N		
Kubo Tech AG	Q		
Kubo Form AG	Q		
Kubo Tech GmbH	R		
West Coast Industrial Supplies Pty Limited	Y		
West Coast Industrial Supplies New Caledonia SAS	AA		
<b>Controls</b>			
IS-Rayfast Limited	A		
IS-Motorsport, Inc.	C		
Amfast Limited <sup>1</sup>	A		
Clarendon Specialty Fasteners Limited	A		
Clarendon Specialty Fasteners, Inc.	B		
Clarendon Engineering Supplies Limited <sup>1</sup>	A		
Cabletec Interconnect Component Systems Limited <sup>1</sup>	A		
Sommer GmbH	H		
Filcon Electronic GmbH	I		
Ascome SARL	U		
Cablecraft Limited	A		
Birch Valley Plastics Limited <sup>1</sup>	A		
Krempfast Limited <sup>2</sup>	A		
Betaduct Limited <sup>1</sup>	A		
Hawco Limited	A		

1 Dormant company.

2 These subsidiaries, which are incorporated in England, are exempt from the requirements of the UK Companies Act 2006 relating to the audit of individual accounts by virtue of section 479A of the Act.

3 These subsidiaries are 90% owned, all other subsidiaries are wholly owned.

All subsidiaries are owned through ordinary shares.

\* Registered Office address

A 12 Charterhouse Square, London, EC1M 6AX, UK.

B 5716 Corsa Avenue, Ste 110, Westlake Village, CA 91362-7354, USA.

C 1201 Orange Street, Ste 600 One Commerce Center, Wilmington, DE 19899, USA.

D 17888 67th Court North, Loxahatchee, FL 33470-2525, USA.

E 4505 Pacific Highway East, Ste C2, Fife, WA 98424-2638, USA.

F 3400 First Canadian Centre, 350-7th Avenue SW, Calgary, Alberta T2P 3N9, Canada.

G Eichsfelder Strasse 1, 40595, Düsseldorf, Germany.

H Kraichgaustrasse 5, D-73765 Neuhausen, Germany.

I Rotwandweg 5, D-82024, Taufkirchen/München, Germany.

J Fort Henry Business Park, Ballina, Co. Tipperary, Ireland.

K Nuolikuja 8, FI-01740, Vantaa, Finland.

L Laki tn 16, Kristiine linnaosa, Tallinn, Harju maakond, 10621, Estonia.

M Maskavas iela 459, Riga, LV-1063, Latvija.

N Vilniaus r. sav., Bukiškio k., Bičiulių g. 29, Lithuania.

O Dom 2, Liter B, Proezd Mebel'nyj, 197374, St. Petersburg, Russia.

P Industrieterrein Dombosch 1, Elftweg 38, 4941 VP Raamsdonksveer, the Netherlands.

Q Im Langhag 5, 8307 Illnau-Effretikon, Switzerland.

R Lederergasse 67, AT-4020 Linz, Austria.

S Bybjergvej 13, DK 3060, Espergaerde, Denmark.

T Industrivägen 17, SE-302, 41 Halmstad, Sweden.

U 10, allée du Vivier, 72700 Allonnes, France.

V 333 Bay St., Suite 2400, Toronto, Ontario M5H 2T6, Canada.

W 226 Lockhart Road, Barrie, Ontario, L4N 9G8, Canada.

X 46 Albert Street, Preston, Victoria, 3072, Australia.

Y 72 Platinum Street, Crestmead, Queensland, 4132, Australia.

Z Office of Bendall &amp; Cant Ltd, Southern Cross Building, 61 High Street, Auckland, New Zealand.

AA 22 Avenue des Géomètres Pionniers, ZAC PANDA - 98835, Dumbéa, New Caledonia.

AB 18 Fuyuangdao Road, Wuqing Development Area, Tianjin, China.



## FINANCIAL CALENDAR AND SHAREHOLDER INFORMATION

**Announcements (provisional dates)**

First Quarter Statement released	16 January 2019
Annual General Meeting (2018)	16 January 2019
Second Quarter Statement released	27 March 2019
Half Year Results announced	13 May 2019
Third Quarter Statement released	28 August 2019
Preliminary Results announced	18 November 2019
Annual Report posted to shareholders	6 December 2019
Annual General Meeting (2019)	15 January 2020

**Dividends (provisional dates)**

Interim announced	13 May 2019
Paid	12 June 2019
Final announced	18 November 2019
Paid (if approved)	22 January 2020

**Annual Report & Accounts**

Copies can be obtained from the Group Company Secretary at the address shown above.

**Share Registrar - Computershare Investor Services PLC**

The Company's Registrar is Computershare Investor Services PLC, The Pavilions, Bridgwater Road, Bristol BS99 6ZZ. Telephone: 0370 7020010. Its website for shareholder enquiries is [www.computershare.co.uk](http://www.computershare.co.uk).

**Shareholders' enquiries**

If you have any enquiry about the Company's business or about something affecting you as a shareholder (other than questions dealt with by Computershare Investor Services PLC) you are invited to contact the Group Company Secretary at the address shown below.

**Group Company Secretary and Registered Office**

AJ Gallagher FCIS, Solicitor, 12 Charterhouse Square, London EC1M 6AX. Telephone: 020 7549 5700. Registered in England and Wales, number 3899848.

**Website**

Diploma's website is [www.diplomaplc.com](http://www.diplomaplc.com).

## ADVISORS

**Investment Bankers**

**Lazard**  
50 Stratton Street  
London W1J 8LL

**Corporate Stockbrokers**

**Numis Securities**  
10 Paternoster Square  
London EC4M 7LT

**Solicitors**

**Ashurst LLP**  
Broadwalk House  
5 Appold Street  
London EC2A 2HA

**Independent Auditor**

**PricewaterhouseCoopers LLP**  
1 Embankment Place  
London WC2N 6RH

**Bankers**

**Barclays Bank PLC**  
1 Churchill Place  
London E14 5HP

**HSBC Bank plc**

City Corporate Banking Centre  
60 Queen Victoria Street  
London EC4N 4TR

## FIVE YEAR RECORD

Year ended 30 September	2018 £m	2017 £m	2016 £m	2015 £m	2014 £m
<b>Revenue</b>	<b>485.1</b>	<b>451.9</b>	<b>382.6</b>	<b>333.8</b>	<b>305.8</b>
<b>Adjusted operating profit</b>	<b>84.9</b>	<b>78.2</b>	<b>65.7</b>	<b>60.3</b>	<b>56.7</b>
Finance expense, net	(0.1)	(0.7)	(0.8)	(0.7)	(0.5)
<b>Adjusted profit before tax</b>	<b>84.8</b>	<b>77.5</b>	<b>64.9</b>	<b>59.6</b>	<b>56.2</b>
Acquisition related charges	(9.6)	(9.7)	(10.3)	(7.4)	(6.4)
CEO transition costs	(2.1)	-	-	-	-
Gain on disposal of assets	-	-	0.7	-	-
Fair value remeasurements	(0.4)	(1.0)	(1.3)	(0.4)	-
<b>Profit before tax</b>	<b>72.7</b>	<b>66.8</b>	<b>54.0</b>	<b>51.8</b>	<b>49.8</b>
Tax expense	(18.3)	(18.6)	(14.9)	(14.4)	(13.7)
<b>Profit for the year</b>	<b>54.4</b>	<b>48.2</b>	<b>39.1</b>	<b>37.4</b>	<b>36.1</b>
<b>Capital structure</b>					
Equity shareholders' funds	291.2	262.0	233.5	189.6	184.4
Minority interest	3.1	4.8	4.3	5.2	2.9
Add/(deduct): cash and cash equivalents	(36.0)	(22.3)	(20.6)	(23.0)	(21.3)
borrowings	-	-	10.0	20.0	-
retirement benefit obligations	10.5	9.9	17.2	9.8	4.3
acquisition liabilities	5.6	6.6	6.8	6.6	4.0
deferred tax, net	8.4	8.2	7.4	5.9	3.3
<b>Reported trading capital employed</b>	<b>282.8</b>	<b>269.2</b>	<b>258.6</b>	<b>214.1</b>	<b>177.6</b>
Add: historic goodwill and acquisition related charges, net of deferred tax	74.6	66.3	59.2	53.6	49.6
<b>Adjusted trading capital employed</b>	<b>357.4</b>	<b>335.5</b>	<b>317.8</b>	<b>267.7</b>	<b>227.2</b>
Net increase/(decrease) in net funds	13.1	11.9	4.9	(17.4)	2.9
Add: dividends paid	27.0	23.7	21.4	19.9	18.4
acquisition of businesses	20.4	20.1	32.7	37.8	16.5
<b>Free cash flow</b>	<b>60.5</b>	<b>55.7</b>	<b>59.0</b>	<b>40.3</b>	<b>37.8</b>
<b>Per ordinary share (pence)</b>					
Basic earnings	47.5	42.0	33.9	32.5	31.4
Adjusted earnings	56.4	49.8	41.9	38.2	36.1
Dividends	25.5	23.0	20.0	18.2	17.0
Total shareholders' equity	257	232	206	167	163
Dividend cover	2.2	2.2	2.1	2.1	2.1
<b>Ratios</b>	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>	<b>%</b>
Return on adjusted trading capital employed ("ROATCE")	24.5	24.0	21.1	23.9	25.8
Working capital:revenue	15.1	15.0	16.6	17.0	17.2
Adjusted operating margin	17.5	17.3	17.2	18.1	18.5

1 Acquisition related charges comprise the amortisation and impairment of acquisition intangible assets, acquisitions expenses and adjustments to deferred consideration.

2 Acquisition liabilities comprise amounts payable for the future purchases of minority interests and deferred consideration.

3 ROATCE represents adjusted operating profit, before acquisition related charges (adjusted for the full year effect of acquisitions and disposals), as a percentage of adjusted trading capital employed. Trading capital employed and adjusted trading capital employed are calculated as defined in note 2 to the consolidated financial statements.

4 Adjusted earnings per share is calculated in accordance with note 9 to the consolidated financial statements.

5 Total shareholders' equity per share has been calculated by dividing equity shareholders' funds by the number of ordinary shares in issue at the year end.

6 Dividend cover is calculated on adjusted earnings as defined in note 2 to the consolidated financial statements.

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