CHIEF FINANCIAL OFFICER'S REPORT

REVENUE GROWTH AND OPERATING MARGIN

	2017 £m	2016 restated £m	Change
Revenue	**411.7**	387.2	+6.3%
Underlying operating profit	**72.6**	68.5	+6.0%
Underlying operating margin	**17.6%**	17.7%	-10bps

	2017 £m	2016 restated £m	Change
UK	**365.7**	338.3	+8.1%
Rest of Europe	**18.9**	17.0	+11.2%
Rest of World	**27.1**	31.9	-15.0%
Group	**411.7**	387.2	+6.3%

UNDERLYING OPERATING PROFIT GROWTH OF

6.0%

UNDERLYING BASIC EARNINGS PER SHARE (p)

10.1%

SUSTAINED INVESTMENT IN STRATEGIC GROWTH OPPORTUNITIES

1.4

TIMES DEPRECIATION

NET DEBT REDUCED TO

1.6

TIMES EBITDA

Group revenue at £411.7m was 6.3% higher than the prior year. With Polypipe France now classified as discontinued there is little foreign currency translation effect on reported revenue, and the structure of the Group on a continuing operations basis is the same in both periods, meaning like-for-like growth was also 6.3%. Within this, revenue derived from the UK market grew 8.1%, with approximately 3.7% driven by price increases and 4.4% by volume growth. This volume growth was materially ahead of the overall UK construction market, which the Construction Products Association (CPA) winter forecast suggests has grown by 3.0% in the year.

The Group underlying operating margin remained robust at 17.6% (2016 restated: 17.7%). The dilutive effect of increasing selling prices to recover absolute cost inflation and the financial performance of our Dubai manufacturing facility has been offset by operational leverage and cost reduction initiatives in our core businesses.

NON-UNDERLYING ITEMS

Non-underlying items in both 2017 and 2016 included non-cash amortisation charges in respect of intangible assets recognised with the acquisitions made during 2015. In 2017, they also included restructuring costs of £4.3m, in respect of the closure of our Dubai manufacturing facility (£4.0m, of which £1.7m is non-cash) and relocation of our Domus Ventilation manufacturing facilities to Nuaire (£0.3m). In 2016, they included a non-cash charge of £0.9m in respect of the impairment of a surplus freehold property that is held-for-sale.

Non-underlying items comprised:

	2017 £m	2016 £m
Amortisation of intangible assets	**5.5**	6.8
Restructuring costs	**4.3**	–
Aborted acquisition costs	**0.3**	–
Impairment of freehold land and buildings	**–**	0.9
Profit on disposal of property, plant and equipment	**–**	(0.3)
Non-underlying items before taxation	**10.1**	7.4
Taxation	**(1.2)**	(1.6)
Non-underlying items after taxation	**8.9**	5.8

Taxation on non-underlying items is covered in the note on taxation below.

DISCONTINUED OPERATIONS

On 31 January 2018, the Group announced that it had entered into exclusive negotiations to sell Polypipe France Holding SAS (Polypipe France) to Ryb S.A., a France-based manufacturer and distributor of plastics in Europe. The cash consideration payable by Ryb S.A. will be €16.5m on a cash-free, debt-free and normalised working capital basis. It was determined that the sale was highly probable at 31 December 2017 and accordingly the net assets of Polypipe France have been classified as held-for-sale in the consolidated balance sheet. In accordance with IFRS 5, Non-current Assets Held-for-Sale and Discontinued Operations, an impairment loss of £12.5m to remeasure the carrying amount of the assets to fair value less costs to sell has been recognised. A loss from discontinued operations of £11.3m (2016 restated: £0.8m profit) is recorded in the income statement, being the impairment loss of £12.5m (2016 restated: £nil), net of the post-tax results of Polypipe France for the period of £1.2m profit (2016 restated: £0.8m profit).

EXCHANGE RATES

The Group is exposed to movements in exchange rates when translating the results of its Mainland Europe operations from Euros to Sterling. Following the EU Referendum in June 2016, Sterling depreciated further against the Euro during 2017 with the average exchange rate used for translation purposes moving from £1:€1.23 in 2016 to £1:€1.15 in 2017. With Polypipe France now classified as discontinued, the impact of this exchange rate movement is now negligible on both reported revenue and underlying operating profit.

The Group trades predominantly in Sterling but has some revenues and costs in other currencies, mainly the US Dollar and the Euro, and takes appropriate forward cover on these flows using forward currency derivative contracts.

Forward foreign currency derivatives are classified as held for trading. There was no unrealised gain or loss on these derivative contracts at 31 December 2017 (2016: £1.5m loss included in financial liabilities). The unrealised gains or losses are treated as underlying and recorded in cost of sales in the income statement.

FINANCE COSTS

Finance costs of £6.9m (2016: £7.6m) were lower than the prior year driven by lower average net debt in the year, and the lower interest rate margin payable on our borrowings as leverage reduces. This reflects the continued cash generative nature of our business. Interest is payable on the revolving credit facility (RCF) at LIBOR plus an interest rate margin ranging from 1.25% to 2.75%. The interest rate margin at 31 December 2017 was 1.75% (2016: 2.00%).

In order to reduce exposure to future increases in interest rates the Group has entered into interest rate swaps at fixed rates ranging between 1.735% and 2.21% (excluding margin) with notional amounts hedged ranging from £60.0m to £91.7m over the period of the interest rate swaps.

The unrealised mark to market adjustment on these forward interest rate swaps at 31 December 2017 was £2.5m negative (2016: £4.2m negative). The movement in the mark to market adjustment during the year of £1.7m is included in the Group Statement of Comprehensive Income.

TAXATION

Underlying taxation:

The underlying tax charge in 2017 was £11.8m representing an effective tax rate of 18.0% (2016 restated: 19.2%). This is below the blended UK standard tax rate of income tax of 19.25% (2016: 20.00%) due primarily to the benefit of patent box relief.

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Taxation on non-underlying items: The non-underlying taxation credit of £1.2m in 2017 represents an effective rate of 11.9%, primarily due to a substantial proportion of restructuring costs being incurred in the Jebel Ali tax-free zone in the Middle East.

EARNINGS PER SHARE FROM CONTINUING OPERATIONS

	2017	2016
Pence per share:		
Basic	22.7	21.8
Underlying basic	27.2	24.7
Diluted	22.5	21.7
Underlying diluted	26.9	24.6

The Directors consider that the underlying earnings per share (EPS) measure provides a better and more consistent indication of the Group's underlying financial performance and more meaningful comparison with prior and future periods to assess trends in our financial performance.

Underlying basic EPS improved by 10.1% in 2017 due to the improved underlying operating result, lower interest costs and lower underlying tax rate as explained above.

DIVIDEND

The final dividend of 7.5 pence per share is being recommended for payment on 25 May 2018 to shareholders on the register at the close of business on 20 April 2018. The ex-dividend date will be 19 April 2018.

Our dividend policy is to pay a minimum of 40% of the Group's annual underlying profit after tax. The Directors intend that the Group will pay the total annual dividend in two tranches, an interim dividend and a final dividend, to be announced at the time of announcement of the interim and preliminary results respectively with the interim dividend being approximately one half of the prior year's final dividend. The Group may revise its dividend policy from time to time.

BALANCE SHEET

The Group's balance sheet is summarised below:

	2017 £m	2016 £m
Property, plant and equipment	98.6	101.0
Goodwill	319.7	329.3
Other intangible assets	36.8	42.3
Net assets classified as held-for-sale	13.1	0.7
Net working capital	0.4	0.5
Taxation	(12.6)	(14.3)
Other current and non-current assets and liabilities	(5.6)	(7.8)
Net debt (loans and borrowings, net of cash and cash equivalents)	(148.4)	(164.3)
Net assets	302.0	287.4

Property, plant and equipment reduced by £2.4m and, excluding the transfer to assets classified as held-for-sale of £9.2m in respect of Polypipe France, increased by £6.8m predominantly due to capital expenditure exceeding depreciation by a similar amount, which included the £3.0m of expenditure deferred from 2016 as discussed in last year's Annual Report and Accounts. Other intangible assets decreased by £5.5m, compared to a decrease of £6.8m in 2016, reflecting that some of the assets in respect of the 2015 acquisitions are now fully amortised. Net working capital reduced by £0.1m but excluding the transfer to assets classified as held-for-sale of £7.2m, increased by £7.1m, driven by higher material costs of inventories and normalisation of stock levels. Net debt is discussed below.

PENSIONS

The Group does not have any defined benefit pension schemes and only has defined contribution pension arrangements in place. Pension costs for the year amounted to £2.7m (2016: £2.5m).

CASH FLOW AND NET DEBT

The Group's cash flow statement is summarised below:

	2017 £m	2016 £m
Operating cash flows before movement in net working capital	90.4	86.7
Add back non-underlying cash items	0.5	–
Underlying operating cash flows before movement in net working capital	90.9	86.7
Movement in net working capital	(10.0)	(0.2)
Underlying cash generated from operations	80.9	86.5
Capital expenditure net of disposals	(23.2)	(18.7)
Underlying cash generated from operations after net capital expenditure	57.7	67.8
Income tax paid	(12.6)	(10.1)
Interest paid	(6.6)	(7.3)
Non-underlying cash items	(0.5)	–
Dividends paid	(21.0)	(17.1)
Purchase of own shares net of option exercise proceeds	(0.7)	(2.9)
Other	(0.4)	(0.4)
Movement in net debt	15.9	30.0

Underlying cash generated from operations after net capital expenditure at £57.7m (2016: £67.8m) represents a conversion rate of 78% (2016: 97%). The lower conversion rate compared to the prior year is due to a higher working capital outflow and higher capital expenditure than the prior year. The higher working capital outflow is largely due to increases in stock, partly driven by higher material costs, and also finished goods stock build. This was necessary to replenish stock back to normal levels in the earlier part of the year following pre-price increase buying in December 2016, and further stock build in the latter part of the year in anticipation of further pre-price increase buying ahead of the February 2018 price increase.

As discussed in last year's Annual Report and Accounts, in a measured response to the uncertainty created by the EU Referendum in June 2016, we took the decision to delay certain capacity expansion capital expenditure projects, while continuing to spend on development growth projects and essential replacement. The performance of the Group since the EU Referendum and the more positive economic outlook compared to the period immediately afterwards gave us the confidence to resume those delayed projects, and therefore net capital expenditure in 2017 at £23.2m was £4.5m higher than the prior year.

In 2016, one million shares were purchased at a cost of £2.9m and held for the purpose of satisfying future employee share option scheme awards. In 2017, a further 748,000 shares were purchased at a cost of £0.7m net of the proceeds from the maturing Sharesave Plan.

Net debt of £148.4m comprised:

	2017 £m	2016 £m	Change £m
Bank loans	**(185.0)**	(192.0)	7.0
Cash and cash equivalents	**35.7**	26.5	9.2
Net debt (excluding unamortised debt issue costs)	**(149.3)**	(165.5)	16.2
Unamortised debt issue costs	**0.9**	1.2	(0.3)
Net debt	**(148.4)**	(164.3)	15.9
Net debt (excluding unamortised debt issue costs): EBITDA	**1.6**	1.9	

At 31 December 2017, liquidity headroom (cash and undrawn committed banking facilities) was substantial and improved to £140.7m (2016: £134.5m) despite the £10.0m contractual reduction in the facility during the year. Continued focus on deleveraging following the Nuaire acquisition in August 2015 has seen our net debt to EBITDA ratio reduce substantially to 1.6 times EBITDA at 31 December 2017 (2016: 1.9 times), demonstrating the continued cash generative nature of our business. This headroom, together with the disposal proceeds from Polypipe France when received, enables us to develop our acquisition pipeline and continue to seek out compelling opportunities to accelerate growth in our strategic development areas.

FINANCING

The Group has an RCF committed through to August 2020 with a facility limit at 31 December 2017 of £290m, reducing by £10m per annum at 31 December 2018 and 2019. At 31 December 2017, £185m of the RCF was drawn down.

The Group is subject to two financial covenants. At 31 December 2017 there was significant headroom:

Covenant:	Covenant requirement	Position at 31 December 2017
Interest cover*	>4.0:1	11.5:1
Leverage†	<3.0:1	1.6:1

* Underlying operating profit: Finance costs excluding debt issue cost amortisation.
† Net debt: EBITDA.

FORWARD-LOOKING STATEMENTS

This report contains various forward-looking statements that reflect management's current views with respect to future events and financial and operational performance. These forward-looking statements involve known and unknown risks, uncertainties, assumptions, estimates and other factors, which may be beyond the Group's control and which may cause actual results or performance to differ materially from those expressed or implied from such forward-looking statements. All statements (including forward-looking statements) contained herein are made and reflect knowledge and information available as of the date of preparation of this report and the Group disclaims any obligation to update any forward-looking statements, whether as a result of new information, future events or results or otherwise. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements due to the inherent uncertainty therein. Nothing in this report should be construed as a profit forecast.

Paul James
Chief Financial Officer