

IMI plc
2022 Preliminary Results

Friday, 3rd March 2023

Introduction

Roy Twite

CEO, IMI plc

Welcome

Good morning everybody and welcome to IMI's 2022 preliminary results presentation. Next slide please.

Strategic execution delivering sustainable growth

This slide covers the key messages from the presentation and the first thing to say is that it was another strong performance in 2022. There is great momentum in the business, we delivered 10% revenue growth. And the Group order book was up 14% - with the Critical orderbook a particular highlight, up 18% at the year end.

Growth Hub is getting stronger and stronger, creating a customer-led, entrepreneurial culture, and really helping to drive the Better World growth that is right at the heart of our strategy. We delivered £52m worth of orders from Growth Hub last year – and I'll give you some exciting examples later on. This cultural change is reflected in our customer satisfaction scores – we are now achieving industry leading benchmarks across the company.

We completed three acquisitions in the year, all in attractive Better World growth markets.

Our adjusted operating margin increased by 80 basis points, as we make further progress towards achieving our through-cycle margin target of 20%.

Employee engagement remains a top priority for the Board and the Exec, and with that I'm very proud to report record scores and a significant reduction in health and safety incidents in the year.

Finally, I am pleased to report that we are increasing the final dividend by 10%, which reflects the Board's continued confidence in the prospects for the business. Ok, so with that I'm going to pass over to Dan please.

Business review

Daniel Shook

Group Finance Director, IMI plc

Revenue and profit growth in all divisions

Thanks Roy, and good morning everyone. I'm pleased to be able to take you through our 2022 results today.

So, an overview of revenue and operating profit. First, as Roy already said, really solid results, organically up 4% on revenue and 8% on operating profit. All three Divisions are up on the top line and increased their margins in the year, with the Group margin up 80 basis points to 17.8%. We continue to manage corporate costs closely, and although the figure is

slightly higher than last year, you'll recall there was a one-off property sale in 2021 which helped us by about £1.5m. For 2023 corporate costs are expected to be around £26 million.

Adjusted EPS increased 15% on last year to 105.5p, at the top end of our previous guidance. Operating cash flow remains strong, and our net debt to EBITDA came in at 1.8x, in line with the guidance we gave in November. So, next slide please.

Third year of profit and margin improvement

Since the launch of our Better World strategy in November 2019, we've made real progress in transforming the organisation, putting the customer at the centre of everything we do, and enabling a culture of sustained, profitable growth. You can see on this slide how, through a combination of strong organic growth and targeted bolt-on acquisitions in attractive market segments, we have delivered three consecutive years of profit and margin improvement. Adjusted operating margins have increased by 360 basis points since 2019. Next slide.

Clear pathway to our 20% margin target

We increased our margin target last year to 20% through-cycle, and as this slide shows given the progress already achieved, we have a clear pathway to deliver on this commitment. Firstly, our complexity reduction programme is progressing well, and is expected to provide a further £42 million of benefits over the next three years. Secondly, Jackie and team are continuing to drive growth in the Aftermarket within Critical Engineering – providing margin support for both the division and the Group. And then finally, continuing our growth in our attractive end markets will provide further margin support. Next slide.

Statutory profit after tax increased by 15%

So, looking at the income statement, as expected the interest charge has increased to £19m, reflecting the increased rate environment and the funding for our acquisitions. We also show a pension finance credit in 2022, but due to the final buy-in on our UK scheme, we expect a small charge in 2023. It means overall finance charge in 2023 will increase to roughly £25 million.

Our adjusting items are broadly in-line with last year, with lower restructuring costs and a hedge gain offsetting higher intangible amortisation and the impact of our exit from Russia.

And finally, taxation – our rate returned to roughly 21% after getting a one-off benefit in 2021. We expect the rate to increase, largely due to the UK rate increase and new minimum tax laws coming into effect. We currently are forecasting a 22% rate for 2023. So, next slide please.

Complexity reduction continues to deliver benefits

Next, an update on our standard complexity reduction programme slide. As you saw on a previous slide, we have delivered sustained margin improvement since 2019 and complexity reduction has played an important role. In 2022 we delivered a further £13m of benefits, ahead of plan – taking the total incremental P&L benefits since the start to £84m. The charge in 2022 was lower than presented at the half year – this is a result of some phasing changes in Critical, with certain project announcements now planned for this year rather than last. There have been no changes to the total costs, and overall, the programme remains on track. As you can see, we expect to complete the projects and deliver the lion's share of the

remaining benefits in the next two years. But as you know we will always look for and execute on opportunities that will enhance the long-term competitiveness of the Group. Next slide please.

Maintaining continued cash discipline

So, continuing to cash flow, where you'll see an improvement versus last year. Working capital was higher, with debtors reflecting our top-line growth, and inventories increasing to support both the significantly higher Critical orderbook and customer service in Precision and Hydronic. Both Hydronic and Precision reduced their stock levels in the second half, although we still are experiencing supply chain challenges within certain parts of these businesses. We will continue to manage our position closely and reduce levels further when conditions enable us to do so without adversely impacting customer service expectations.

Capex of £71m is about 1.2x depreciation and includes investments to support growth and our sustainability ambitions. We continue to see good opportunities to deploy capital into our core businesses to drive further performance improvement.

Our net debt has increased to £812m at the year end, reflecting in-year acquisitions but also an adverse FX movement of around £50m due to our US and Euro debt positions. Net debt to EBITDA remains within our target range, and we continue to develop an attractive pipeline of bolt-on acquisitions.

IMI Precision Engineering: Continued strategic progress, targeted M&A

Okay, so getting into the divisional performance, Precision had an excellent 2022 - adjusted revenue was up 18% with organic growth up 5%. Profits are 23% higher, and margins improved by 70 basis points to 18.5%. Running through the sectors:

Industrial Automation's organic revenue was up 7%, with the integration of Bahr progressing really nicely.

Process Control organic revenue was up double digits at 16%

Life Sciences revenue was down 8% organically, although do remember that we had the last of the ventilator surge sales, about £12 million, in the first few months of 2021. Life Sciences grew organically by 10% if you exclude those surge sales. Now, adjusted revenue is up significantly due to the Adaptas acquisition, which is performing very strongly. Its order book at the end of 2022 was £16m higher than at the start of the year, a 66% increase, and the growth opportunities being identified from the collaboration between Adaptas and IMI's existing Life Science businesses are significant and growing.

Commercial Vehicle revenue was down 1% in the year - with positive results in Europe and the Americas offsetting Asia which was heavily impacted by China's Covid lockdown. We still see business being held back by component shortages but maintain our strong relationships with OEMs which position us well to meet demand when these pressures ease.

Our Rail business continues to trade well, delivering 12% organic revenue growth in the year. We are tapping into very good growth opportunities, particularly in Asia, where our solutions significantly enhance the safety of passengers during their journeys.

Before moving to the outlook, I wanted to highlight the important evolution of Precision's business since 2009. Our sector businesses have grown from roughly 30% of revenue to over

50% now, reducing our exposure to the cyclicity of general industrial production. In addition, Beth and the team continue to build out Industrial Automation's Aftermarket, which now represents around 40% of IA revenues.

So finally, the 2023 outlook. Based on current market conditions, including the softening industrial production environment, we expect Precision Engineering's organic revenues to be lower than in 2022 with margins slightly higher. So next slide.

IMI Critical Engineering: Record order book, further progress on margins

Critical had an outstanding 2022, with strong order intake, continued organic growth and margin expansion. Orders were up 12% in the year, led by a 16% increase in Aftermarket. The Energy end markets – particularly upstream oil and gas, including LNG, delivered well. New products are playing a big part in Critical's growth, with £43m of Growth Hub orders in the year.

Organic revenue was 2% higher than the prior period, and 3% higher on an adjusted basis. Margins are up 90 basis points and now at 19%, reflecting the division's action to reduce complexity and its continued evolution toward a more Aftermarket intensive business. You can see in the top right how Aftermarket orders have grown at an 8% compound annual growth rate since we launched the strategy in 2019.

Critical ending orderbook is up 18%. We saw significant New Construction activity in the second half of last year and given the longer lead times we expect much of those orders won't ship until 2024. Therefore, on outlook, based on current market conditions, we expect 2023 organic revenues to be up high single digits. Margins are also expected to be higher. Next slide.

IMI Hydronic Engineering: Continued growth and margin expansion

Onto Hydronic Engineering. A solid performance from Phil and the team, with 4% organic growth against a stronger 2021 comparator given the installer catch up activity post COVID. We continue to see strong demand for our energy saving solutions, like our Halo-B thermostatic radiator valve which Roy will highlight shortly. Although we cannot fully quantify, we know there was some distributor de-stocking in the second half of last year. Hydronic's on-time delivery remains consistently above 90%, which is excellent performance but does mean our customers can get comfortable holding less stock.

Operating Profit is up 5% organically and the division continues to invest for the future while remaining a 20%+ margin business.

In terms of outlook – based on current conditions, we expect Hydronic Engineering's 2023 organic revenues to be higher supported by demand for our energy saving solutions. Margins are expected to be higher, supported by the Heatmiser acquisition. Next Slide.

UK pension now fully de-risked

Now we have bought the pensions slide out of the appendix as there is some news – two things, really. First, we completed a final buy in of the remaining UK pension liabilities in December last year. This has fully de-risked the UK DB pension scheme. Many of you will remember when we started this journey back in 2014 with an overall UK liability of £1.3 billion. Through a series of buy-ins and buy-outs, we have managed the position, and the

risk, down. We will now assess the merits of a final buy-out in 2023, which would remove the remaining UK asset and liability from our balance sheet.

Second, as a result of this buy-in and the adequately funded position, we have stopped the previously required £7 million annual contribution, so we are seeing an immediate cash flow benefit of £7m going forward.

The overseas schemes will be the focus of the team going forward, where we will continue to look for opportunities to reduce our outstanding liabilities. Next slide.

Continued disciplined approach to capital allocation

We thought it was a good time to remind everyone about our capital allocation principles.

We look to maintain a very disciplined approach to capital deployment. Given the diversity and resilience of our businesses, we target a debt/EBITDA position of between 1x and 2x. The cash generative nature of our businesses means our leverage level should reduce by about half a turn during 2023, unless we are successful with additional acquisitions to accelerate our performance.

Capital investment continues to be an important driver of sustainable profitable growth. We focus on Better World opportunities and expect to continue to spend at a level above depreciation. Operating expense investment is equally important, with R&D expenditure exceeding 3% of sales in 2022. This figure still does not fully reflect all the Growth Hub activity around the Group - it truly is embedded into everything we do now.

On acquisitions, we will continue to pursue those that help us move further into attractive markets, and we will execute them within our strict return guidance – delivering IMI's cost of capital by year three and to not be materially dilutive to the Group's overall ROIC by year five.

And finally, we manage our debt position to minimise both the interest rate and liquidity risk, maintaining roughly 75% of our debt at fixed rates, which are currently fixed at about 3%. And we have spread the maturities of this debt over six years, starting in 2025.

Group outlook

Now the final slide before I hand over to Roy – the Group outlook statement. Based on current market conditions, we currently expect adjusted EPS to be around 111p in 2023. That's considering a net interest charge of around £25m, a 22% tax rate and assuming FX creates a tailwind of around 2%. So with that, let me hand back to Roy to take you through the strategy update. Thanks everyone.

Strategy update

Roy Twite

CEO, IMI plc

Delivering on our strategy

Thank you, Dan. This slide clearly shows how our strategy is delivering sustainable improvements in our financial KPIs since the strategy was launched in 2019.

Revenue has been growing at 3% CAGR, our operating margin is up 360 basis points at 17.8% and adjusted profit before tax has been growing double digits at an 11% CAGR.

ROIC has improved by 130 basis points to 12.7% and adjusted EPS has increased from 73.2p to 105.5p.

Next slide please.

Purpose-led strategy solves acute customer problems

I wanted to provide a quick refresher on our strategy. At the heart of the strategy is our purpose, Breakthrough Engineering for a Better World. This is an incredibly powerful driver, which has unleashed the tremendous energy of our people to solve key industry problems, helping our customers become safer, helping them become more sustainable and more productive.

There are three key pillars to our strategy:

The first is customer satisfaction. We provide world class engineering expertise, and excellent service to all our customers, alongside deep sector knowledge and know-how. Our focus is on solving our customers' problems. We have market leading brands and we are achieving industry leading customer satisfaction scores across IMI.

The second is market-led innovation. Our innovation incubator, Growth Hub, supported by selective M&A, enables us to develop breakthrough solutions to support our customers with their most challenging and complex engineering problems.

The third is complexity reduction. We continue to simplify and improve our global manufacturing footprint and demonstrate a resilient supply chain to support our customers.

Next slide please.

Aligned to attractive markets supported by macro trends

Our three divisions are aligned to attractive growth markets and we have a portfolio that is supported by global macro trends. The long-term fundamentals in each of these key markets are strong and we have the ability to make a significant, positive impact.

I am going to highlight a few examples. In Life Sciences, the global health threats we face, along with the rapidly improving approach to diagnosis and treatment, presents a huge opportunity for us. We can empower our customers by helping to automate their processes to diagnose disease early and support highly tailored, patient-focused critical care.

In Indoor Climate, the global drive to net zero, along with the increased energy prices, means that more than ever, our customers need to reduce energy consumption, improve building comfort and combat climate change. Heatmiser is a really exciting acquisition for us in this space.

Next slide please.

Better World growth strategy delivering orders

Growth Hub remains absolutely at the heart of our Better World strategy, and I'm really pleased to report that a record £52m of orders were won through Growth Hub last year. Pipelines remain really healthy across all three divisions and more and more employees are

getting involved, taking the knowledge that they gain back and applying it in our core business to create more value today.

Whilst there were nine Growth Hub projects that delivered over £1m of orders last year, I would like to highlight three specific Better World projects that really demonstrate the commercial mindset and customer-focused culture that Growth Hub is fostering within IMI.

Firstly, our focus on hydrogen as a sustainable fuel is leading to a number of exciting early project wins. Our HydroGreen team are actively supporting the development of hydrogen refuelling infrastructure with solutions that reduce the cost of operating refuelling stations – they secured £3m of orders in last year and we expect that to double this year.

Secondly, you may remember we introduced EroSolve at our Capital Markets Day back in 2021. EroSolve is an innovative solution that prevents steam erosion in process industries, minimising plant downtime and extending plant life – improving efficiency and return on investment for our customers. It is now a significant driver of growth and we secured £17m of orders last year.

Finally, our Halo-B thermostatic radiator valve is a great energy-saving new product. You might be aware that Germany have issued a regulation limiting the temperature of municipal buildings to 19°C this winter – this is a very effective way to save energy, a one degree Celsius decrease in temperature can reduce energy consumption of the building by around 6%. After seeing this policy announced our team quickly developed the Halo-B valve which helps limit the temperature in a building to 19°C - this has been a great success in Germany and we secured £4m worth of orders in the year.

Hopefully these examples provide you with a good feeling for how our Better World strategy is really accelerating organic growth.

Next slide please.

Acquisitions accelerating Better World growth

As you know, we have completed four strategic acquisitions since December 2021, and on this slide I'd like to provide a very quick update on how things are going.

Adaptas has traded very strongly since we acquired it in December 2021. We continue to see a great opportunity to cross-sell Adaptas's leading mass spectrometry technology into our existing OEM customer base and vice versa.

Adaptas has been further complemented by the acquisition of CorSolutions, another Life Sciences business, where we are already seeing very strong customer demand, and a significant opportunity to scale up.

The integration of Bahr is on track. We are actively progressing with our plan to rapidly scale Bahr's high added value products and systems through our Norgren sales network.

Finally, we completed the acquisition of Heatmiser, the UK leader in smart thermostatic control, in December 2022. Heatmiser provides a unique opportunity to accelerate our growth in smart buildings and we are very excited to scale Heatmiser's predominantly UK based business across Hydronic's core markets.

All four acquisitions present the opportunity for significant synergies and are on track to deliver and growth and financial targets. Next slide please.

ESG: Creating a Better World

I also wanted to take this opportunity to give you an update on our ESG progress and provide an overview of our new sustainability framework – Creating a Better World.

This framework sets out the most important priorities for our business and it has been developed in collaboration with our stakeholders who were part of our materiality assessment.

There are three pillars to this framework.

Firstly, empowering people – we develop and empower people to make an impact and to create a better working world. We have made great progress in the year, with employee engagement now at record levels and our recordable accident rate improving by 38%. We are also making good progress on gender diversity and are benefiting from the strong female representation on our Executive Committee and Board.

Secondly, sustainable solutions – we engineer solutions for our customers that are safer and more sustainable. Every day our people are helping to improve energy efficiency in buildings, improve analytical devices to save lives, and reduce emissions in both oil and gas, and in trucks.

Thirdly, climate action – we play our part to address climate change and protect the planet by minimising the environmental impact across everything that we do in IMI. We continue to see great progress in reducing our CO2 intensity, with a 9% reduction last year and 25% since 2019. We are committed to a net zero target for Scope 1 & 2 emissions by 2040 and are very pleased to announce a target to be net zero for Scope 3 by 2050.

Next slide please.

Key messages

To summarise then, the key takeaways from today are:

First, that our purpose-led strategy that we set out in late 2019 continues to deliver, with 4% organic revenue growth, 15% adjusted EPS growth and the order book up in all divisions.

At the heart of our strategy is our Growth Hub, which is going from strength to strength – and delivered a record £52m orders in 2022, while fostering a customer-led, entrepreneurial culture.

Third, we have completed four strategic acquisitions since December 2021 – all of which are in attractive Better World markets and present opportunities for growth.

Fourth, as Dan said – we expect this year's EPS to be around 111p and remain on track to deliver our ambition of sustainable, profitable growth and a 20% through-cycle operating margin.

Okay. So with that, I'm going to stop talking there and turn over to the moderator for the Q&A.

Q&A

Operator: And our first question today goes to Andrew Douglas from Jefferies. Andrew, please go ahead, your line is open.

Andrew Douglas (Jefferies): Good morning, gents, thank you for the presentation. I've got three questions, two should be really quick, and hopefully one will also be quick. On Precision, I'm just interested in your commentary on the outlook for Industrial Automation. I know that you're historically a PMI business. But one or two of your peer group, who are also PMI-correlated, are talking about reasonably healthy growth in IA. Can I just double-check, is this typical IMI conservatism? Is there any kind of market share loss that we need to be aware of, or anything else that you can give us there? It just feels like that's potentially a little bit soft, but I'll leave you to discuss that.

Secondly, on pricing, clearly, lots of ups and downs when we think about the whole pricing equation. Can you just give us a view on whether we should be modelling prices up this year and whether that's an annualisation of last year's numbers or are you putting more prices through this year?

And last but not least, on Growth Hub, clearly £52 million of orders is great. Are you looking to expand that in the current year? So, any guidance there would be helpful. Thank you.

Roy Twite: Great. Well, thanks, Andy.

Yeah, Precision. So, on Precision, we certainly don't feel we're losing market share, Andy. Our customer satisfaction scores, for instance, are now industry-leading, right? So, we use Net Promoter Score and we're up there in the 40s, so we definitely don't feel that. I think, with us, Andy, we will pick a forecast that we think is absolutely achievable. With IA, what we've done is look at PMIs, we looked to previous recessions, and we've used that. And it's very important for us, as we manage the business to make sure that we get our costs in line. And as you see, although we're forecasting Precision to be down in terms of sales, we're forecasting it up in terms of margin.

So, managing our cost base is very, very important for us and making sure that we can show the benefits of the restructuring, as we have done since 2019. And as Dan said in his presentation, delivered over £80 million of benefits. And as you can see, profit since the 2019 result and the strategy presentation, up nearly £100 million in those three years.

So yeah, that's how we run the business. We want to make sure that the costs are in line. The other people could well be right. I mean, it's certainly only early trading. January, February is solid, right, within Precision.

Andrew Douglas: Yeah.

Roy Twite: So, you know, they could well be right. But for us, we don't want to rely on any sort of better outcome. We want to make sure that if we do get a better outcome, Precision, of course, is a high added value business. As I said many times, I was managing it, as we came through the – through 2009 and through the other side, and we got tremendous drop-through in terms of the profit. So – and that's the way we want to run the business, right? We

want to make sure that we are prudent, we're careful, we don't rely on any sort of second-half recovery.

I think some of the peers have got a point. And again, it's not clear to us because we get a mixed picture. Obviously, out there right now, labour costs are high, right? And labour's difficult to get hold of, and that is making people think about automation, there's no doubt about it. So, the question will be, does reduced consumer spending because of inflation, and energy costs and everting else, mean that capital starts to come down, capital spend starts to come down.

At the moment, as I said, Andy, we're solid. And we really hope that everybody else is right, but we don't rely on hope. We make sure we get our costs in line, and if we get that extra sales, we'll be obviously absolutely delighted – and I'm sure everybody will be.

So, that was the first question, I think. Dan, do you want to cover pricing?

Daniel Shook: Yeah, sure. Hey, Andy. I mean, we did get good pricing, and I think last year was a lot around managing the input cost, commodities and components, and got that nicely, and you saw the result on the margins. We probably have about two percentage points of carry-over. And as you know, there's probably a bit more pricing in Hydronic and a bit less in Critical. And off that base, our expectation is we will need to move pricing further in 2023, and that's more down, as Roy already just mentioned, to the labour pressures and labour inflation. So, we'll look to make sure we manage that, and clearly use all of the productivity as well to manage that as well. So, looking for further price movement as we get through 2023.

Roy Twite: Yeah, I'll just add to that, Dan. I think Dan's absolutely right. I think pricing this year will be mid-single digit, Andy, and it will be obviously predicated more on labour inflation. Last year, it was more material inflation. And as Dan said, probably at least 2% of that is carry-over. And actually, most of the rest of it is now agreed. So, we're pretty sure that, that is going to come through.

And then Growth Hub, Andy, was your last question. Yes, I mean, first of all, delighted with what's happening with Growth Hub. I think it's really cultural, Andy. It's the most important thing, right? Because we can look at those orders, and they're important from those teams really, really important to us that we can generate market-led innovation, that we can go out, solve customer problems, create solutions quickly. And as I showed some examples, I love that Halo-B example because the teams reacted so quickly. The German government said 19 degrees in municipal buildings because they need the energy saving. Our team reacted, scaled up more than 10 times. It was a bit like the ventilator challenge in my mind.

The teams are so responsive, so market-facing and that's what's key. And actually, even that Halo-B order is about £4 million, it's not even in the Growth Hub numbers, right, because it wasn't done through all of the Growth Hub techniques, but it's another indication of how the culture is changing in the company. And that's why I'm actually trying to move away a little, Andy, from just Growth Hub target, because I want the whole company to react like that, right?

Deeply cultural, deeply based on our customers' needs. And not on what we've got and try to sell that; much more on, we can solve your problem, we react to you. And that's why,

obviously, the Net Promoter Scores, customer satisfaction scores are going up. And that culture for the company will lead to higher growth, and that's what we want to keep accelerating, that overall growth level, Andy.

So yeah, no, really good news. And yeah, we're pleased with it.

Does that answer your question, Andy?

Andrew Douglas: Yeah, that's great. Thank you, guys. Thank you very much.

Roy Twite: Thanks a lot. Cheers.

Operator: Thank you. And the next question goes to Christian Hinderaker of Goldman Sachs. Christian, please go ahead, your line is open.

Christian Hinderaker (Goldman Sachs): Yes. Good morning, everyone, and thank you for the opportunity to have questions.

I just wanted to come back to the margin expansion that you see across all three of your divisions. That's obviously encouraging. We know about the £20 million of restructuring savings, and you've talked a little bit about pricing. But I guess just to narrow in on that a little further, you mentioned wage inflation. Some companies here in the sector are talking about 5%, 6%, 7% cost inflation on the labour line. What do you see in terms of that inflation rate? And also more broadly, are there any considerations in the bridge to think about with regard to, say, M&A in terms of those margin expectations? And then I'll come back to the other two.

Roy Twite: Thanks, Christian. Yeah, I think obviously, we're seeing similar levels of labour inflation, right? We want to keep all our best people. We want stability in our workforce and, broadly, that's what we've got now. And we want to keep that. It's very, very valuable to us. So yeah, similar levels, as I said, pricing matching that, though, we expect to win the overall inflation equation. We are seeing a bit of relief on some materials, and that will help us compared to the high levels of inflation last year. So, that's good news on the materials side.

Roughly, our P&L is sort of just over 30% labour, just over 30% materials. So, that's pretty equally balanced. So, a bit of relief on materials is good.

And, of course, we've got our own efficiencies that we're driving as well, plus the £20 million from the programmes. The good news on the programmes is the vast majority of that is now done for the £20 million, which is great. That was three big site consolidations in Precision. And I think Beth and the team have done a great job in terms of making sure those projects have been done on time to budget. And we're starting to see the savings coming through in the P&L already. So, that's encouraging, Christian.

So, I think overall, in terms of inflation, the bridge, yeah, it will be helped by, obviously, the accretive margins on the acquisitions. But in the overall scheme of things, that's relatively small. Heatmiser obviously does help Hydronic. Probably that's the big one, really, Christian, in your models and that is worth about 100 basis points for Hydronic. It's obviously not for the Group. It's not that big, unfortunately. But yeah, Hydronic is worth 100 basis points.

So, Dan, anything I missed in that bridge?

Daniel Shook: No. No. I mean, that's why I presented it. I think we see a clear shot to getting ourselves up to that 20% through the cycle. I think also that gives us, as we continue

to deliver close to that, the opportunity to continue to invest in the business to drive the top-line growth as well organically. I think that's the key for us. As we approach that number and get there, we'll want to make sure we're continuing to invest in the Growth Hub teams but across the business in the Better World segments.

Roy Twite: It's a really good point actually, and it's point I should have made. We've improved profits by nearly £100 million over the last three years despite a lot more investment in the business, despite the fact that 800 people have been contributing over that period of time into Growth Hub, despite the fact that R&D as a percentage of sales has gone up from just over 2% to just over 3%. So yeah, I mean, we are investing heavily. We want this business to grow faster. I mean, that's our main activity. And that obviously contributes towards achieving those 20% margins.

Christian Hinderaker: Okay. Thank you, both. Maybe just turning – so you mentioned ongoing supply chain issues, I think, in Critical and Precision. I just wondered if you could elaborate on that in terms of magnitude, whether it's specific product categories or any regions in focus. It seems that peers in the market have seen a better situation in supply relative to, say, six months ago?

Roy Twite: Sorry, I sort of missed the early part of that question.

Daniel Shook: Just elaborating on the supply chain. I think, yeah. Certainly, the boats are moving a lot faster around the world now, and the ports have kind of caught up. We're not necessarily seeing lead times come down across all the elements. And well, I would say though that in certain parts of our business, our customers have started to destock as they get confident because of our performance. And as you know, Christian, we are moving more and more towards a local-for-local supply chain. We continue to look for ways to bring our products and produce them in-country. So, I suspect we're continuing to watch it.

It's still within, I'd say, elements of Hydronic, some components that we do take out of China into other parts of the world. And in Precision, there are some elements that do cross the long-term borders. It is improving, but we're not going to declare victory just yet, and we're going to continue to maximise and focus on giving the customers, the right on time delivery and the right performance. But having said that, I suspect as we go through the year, subject to all of that, we'll look to bring some of those stock levels down and deliver an improved cash conversion for 2023.

Roy Twite: Yeah, completely, agrees.

Daniel Shook: Does that cover your question?

Christian Hinderaker: So, it's not – yeah. So, it's not specific to say, to commercial vehicles within Precision or particular end markets, it's more broad-based shipping issue. Is that right?

Roy Twite: Yeah. I'd say electronics are still the most affected components, right? So, as Dan said, that affects parts of Hydronic, parts of Precision. And outside of that, as Dan said, lead times generally from supplier – transport lead times have come down, no doubt, as Dan said. The boats are definitely much better, right? Transport costs have come down. But in terms of supplier lead times, we are not seeing a dramatic reduction in supplier lead times yet. Some suppliers are still reporting hard to get hold of additional labour, but they are also reporting that they would like to start quoting for more new business as well, right, which is

always a sign that they think capacity is going to get freed up in the – in say, the short-term future Christian, right?

So, I think what we're going to see, and certainly talking to one of our lead Supply Chain Directors, he was thinking, sort of, end of Q2, Q3, we probably start to see the effects of shorter lead times. But he did put one proviso in, which is that China opening up, which is obviously a good thing in terms of markets, doesn't suddenly soak up a lot of capacity. So, that's the only rider on that, Christian.

Christian Hinderaker: Thank you, both. And then, third and finally, Dan, you touched on cash conversion. I just wondered what level of free cash improvement you might expect along with the margin expansion this year. I think you've had around £136 million of cash out from working capital in the past two years. And then prior to that, an inflow of around mid-teens in terms of the £1 million mark. What would be a reasonable expectation for working capital improvements as we move through this year?

Daniel Shook: Yeah. I'm going to shy away from giving an absolute target number. What I can say is we delivered 80% cash conversion this past year, and again, continue to put the stocks in to cover off the supply chains. I'd expect as we go through the year and based on what we see today, the cash conversion for 2023 is going to be, kind of, in the 90% range. Again, we are going to make the investments also on the CAPEX side and continue to deploy capital that way as well. So yeah, and I think that's probably where we wanted to get to. So, we make sure we're continuing to invest in the business. So, yeah. So, a targeted cash conversion, kind of, as we – as everything normalises and around the 90% range feels about right. And that's what we're targeting right now, Christian.

Christian Hinderaker: Okay. Thank you.

Daniel Shook: Brilliant. Thanks.

Roy Twite: Thanks, Christian.

Operator: Thank you. And the next question goes to Andrew Wilson of JP Morgan. Andrew, please go ahead, your line is open.

Andrew Wilson (JP Morgan): Hi. Good morning, everyone. Thanks for taking my questions. I'll stick to two. I wanted to start on – it's maybe a follow-up to a couple of comments you made, one in your prepared comments and one to Andy Douglas's question. But just on Hydronic in terms of the destocking, which you talked about, can you talk about where you think customers are in that, and if you've seen any change? And I guess linked to that, have you seen any of the same effects in Precision because I'm conscious that clearly, that can have moved around a little bit, and maybe customers had restocked earlier in the year. So just trying to get a sense of kind of both of those dynamics, please.

Roy Twite: Yeah, good point, Andy. Yeah. So, I mean, Hydronic, you saw Hydronic slow significantly in the fourth quarter. That was certainly wholesaler destocking. We've had conversations with those wholesalers, and they have their own cash targets to achieve. Dan actually met personally with one of those wholesalers. So, we've got pretty good data on what happened. And the good news, Andy, is that as we come to January and February trading, that has clearly stopped now. So, I wouldn't say it's definitely all done. But as far as

we can tell, the vast majority of the destocking in Hydronic is done, which is obviously good news.

As Dan said, Phil and the team, just done a tremendous job. I mean, they kept on-time delivery pretty much throughout COVID at around 95%, always over 90%, and that was partly because of what they did operationally. And you'll remember they consolidated three warehouses into one, which gives us better stock profiles, better coverage. But also operationally, they're doing a fantastic job. So very, very good. That's where we want to be. The Net Promoter Scores are fantastic. Customer service also are fantastic. But obviously, that means that our wholesalers can take stock down and be comfortable that we'll still deliver. So, that's definitely what happened in Hydronic, and that definitely reduced Hydronic's growth last year.

And I would think, Andy, a similar thing has happened in Precision. Obviously, Precision way up in IA in the first half last year, pretty flat in the second half. And because we're a component supplier, we're on the end of the supply chain, and it always happens if you look at Precision's history; on the way up, we'll get better growth, on the way down – remember, part of what we do, particularly in IA, is through distribution, and they will tend to adjust stocks accordingly when they see tougher times are coming. So yeah, I think you're absolutely right in terms of what's happened there, Andy.

Andrew Wilson: Thank you. And in terms of Critical and just thinking about the outlook for 2023, obviously, you provide some – again, have provided very helpful comments by, sort of, end market last year. I'm just interested in terms of the thought processes in terms of the big end markets for Critical in terms of orders? Because clearly, there was a very, very good momentum in 2023. How sustained – how sustainable is another the year of growth if we think about specifically orders? Obviously, sales are very well underpinned, but orders for Critical in 2023?

Roy Twite: Yeah. I mean, our plan is for all this orders, you know, all things being equal, to be up again this year on last year. And again, Jackie is winning. I mean, you could see fourth quarter is super strong, right, which is why we think sort of sales up this year high-single digit rather than the full order book. Because, obviously, as you know, a lot of those orders will be 12 months, a bit longer, you know, fall into 2024. So, we think Critical is in great shape.

Aftermarket strength as well, Andy, really coming through very strong. Part of that's on the back of the Growth Hub work that Jackie has absolutely driven and actually improved. It's what I love about that team is that they take the concepts and actually take them forward very, very quickly.

So yeah, we actually think orders will be up this year. Clearly, you can see it's oil and gas strength. Talking to Jackie, he feels that this year will be another strong year for LNG upstream. Similar to last year, there's projects out there, we're getting high hit rates. And then what normally happens is, and I think Jackie is right in this, is that you then get downstream strength, right? And that sort of follows on for the period after that. So, as you know, we're strong in both areas, and we feel pretty good.

There's also, actually, a lot of conventional power going into China as well over the next three or so years, and we're well-placed with that because that's going to be the most sophisticated sort of power stations where we're very competitive, as you know. So yeah, our installed base

went up last year. Parts went up. And that, I think we're doing about £250 million now worth of parts business a year at very good margins, as you know, Andy.

So yeah, all in all, I think we feel good about Critical, and we feel good that orders should go up again this year.

Andrew Wilson: Very clear. Thank you, guys.

Roy Twite: Thanks, Andy.

Operator: Thank you. And the next question goes to Mark Fielding of RBC. Mark, please go ahead, your line is open.

Mark Fielding (RBC): Yeah. Morning, guys, thanks for taking the question. Just – actually, first, can I just follow up on with – you know, talking with Andy there about the Critical outlook? And I suppose I'm curious on a bigger picture. I mean your Capital Markets Day a couple of years ago, obviously, it was the lowest of the three growth targets you set for the divisions. The world has obviously taken a significant shift since then, in terms of energy crisis, etc. Just thinking about how you think about the sort of medium-term growth dynamics of that business now?

And then maybe a more specific question on that, which is, if the OE orders that are coming in now and things are more about 2024, just, I suppose, how do we think about the margin dynamic over the next couple of years? Because at the minute, as you said, a big part of your list to 20% margins, or one part of that list is the Critical Aftermarket growth, but there is this period where not a bad thing in any way, OE might accelerate ahead of the Aftermarket?

Roy Twite: Yeah, it's a good point. Yeah.

Daniel Shook: Yeah.

Roy Twite: Yeah. I think, well, first of all, in terms of Critical outlook, since the Capital Markets Day, yeah, it's changed quite fundamentally. I think energy security has risen to the top of the list for many, many countries. And obviously, LNG as a cleaner transition fuel has become a fundamental part of that, and one of our real strengths is LNG. So, I think, yeah, you'd have to say the outlook for the medium term is good, actually.

I've seen some numbers from one of our big peers projecting huge increase in LNG capacity up till 2030. And it's hard to sort of disagree with that now. So yeah, I think if we were doing that Capital Markets Day, again, Mark, we'd probably have a slightly different view. But – so I think where is Critical, it's great.

I think beyond the medium term, Critical's strategy is to really make sure that we win in the installed base. And that's what they've done fantastically. I mean Aftermarket orders last year were up 16%, as you know, Mark. So, I think that's still a fundamental thing. And we drive so much of the future profits of that business from the Aftermarket, that if we can grow that way beyond any next oil and gas surges on New Construction, then that business has got, I think, a fantastic future because we think the installed base will obviously be there for decades, right? And that's got to be good news.

The other thing I would say is that the factories are in really good shape. And during Mark's time, as you know, we focused heavily on the factories. And within Critical, we consolidated the number of factories. We basically halved it, right? We went from sort of 30 to about 16 I

think it was. And the 16 we put it in were the better factories. Obviously, they were more operationally efficient. They're better at continuous improvement. They're more customer-focused. And as we drop New Construction business in there, it will flow through to the bottom line. And I don't see a massive dilutive effect from that actually.

What I do see is an accretive effect from the increase in Aftermarket. Plus, as you know, we talked about this year's £20 million worth of rationalisation benefits. Actually, remember that in total, we've got about £42 million to come, as Dan said, when he presented his chart. And a big chunk of that second £22 million is going to come in Critical. So, you know – and we see that really starting to kick in next year to really underpin their margin performance as well into the future.

So, no, I think we feel good about Critical, and we feel good about a 20%+ margin target in Critical through that medium term. So yes, I think it's in a good place.

Mark Fielding: Thanks. And actually, can I just ask a sort of slightly related follow-on, in terms of the wider restructuring plan? I mean, it feels like you stuck out another roughly adding in the 2022 and then after a year it's about another £5 million of extra benefits from the plan in the announcement today. And I suppose, do you feel like once you get to the end of this 2024, little bit in 2025, but always there's obviously continuous improvement? Will that be largely it when we're thinking about the restructuring benefits and also restructuring costs?

Roy Twite: Yeah. I think, as you know, we set out a plan, and we've increased the margin targets, and we increased the spend a bit on that plan. But fundamentally, it was the plan we set out back in 2019, and that will dramatically reduce the complexity of the business. So, as I said, in terms of the number of sites, right? So putting it into our best sites does so much more than deliver those benefits in the P&L. It massively reduces our complexity.

And I can remember a chart back in, I think it was 2013, showing our supply chain. Now, much of that is being consolidated. That big German plant that we just consolidated into Brno was a huge part of that supply chain complexity. So, it's much more than about those short-term benefits. It's about the long-term growth and success of this business. But we – as Dan said, we will always look for opportunity. I don't think they'll be up - we'll be spending the sort of money that we've been spending per year. But could we spend something like, I don't know, £15 million, Mark, on a project that would again give us more benefits, of course, we could do that. And we wouldn't walk past it because, again, we want to grow faster. We want to keep taking the complexity out of the business. But largely, this particular programme will be done, yeah.

Daniel Shook: And I'd just say as we go forward, M&A sometimes gives rise to further moves as well. In the Adaptas case, we acquired a wonderful, wonderful business and a wonderful campus. And we've actually been able to move some of our activity into Palmer, Massachusetts. That's gone really, really well. So, that's the other caveat, I'd say, Mark, as we bring further bolt-ons into the family, that could be another option.

Roy Twite: If they are a multiple site. I mean, the ones that are a single site, obviously, we're buying them for their tech and for their growth. Heatmiser, we absolutely want to build on that site and invest in it. It's just fantastic in terms of smart buildings. So yeah, but multiple sites, those sort of complex acquisitions, we'd certainly look at the opportunity, yeah.

Mark Fielding: Great. Thank you very much.

Roy Twite: Thank you.

Daniel Shook: Thanks, Mark.

Operator: Thank you. And the next question goes to Jonathan Hurn of Barclays. Jonathan, please go ahead, your line is open.

Jonathan Hurn (Barclays): Hey guys, good morning. I have three questions, please. Just one on Industrial Automation, and two on Critical.

Firstly, just on Industrial Automation. Can you just talk about the 40% of sales that are taken from Aftermarket? And essentially, how that sort of Aftermarket sort of trades through the cycle? Is there a lot more resilience for you versus the OE?

Roy Twite: Yeah. No, Jonathan, absolutely, it is. It's higher margin, and it's definitely more resilient. So, you definitely find that people are obviously keeping their own kit running. They're not necessarily investing in new production lines. But generally, unless it's a super severe recession, I can only think of one of those, they continue to buy all the spare parts, absolutely. And so, that 40% is part of the reason that we think that Precision would be a more resilient business this time.

Jonathan Hurn: That's very clear. And then the same question, just on Critical. Just coming back to the margin there. I think if you look at the chart that you put up on slide eight, obviously, you've got about £15 million savings to come through from that over the next few years. If you kind of put that into Critical, it would kind of imply a margin of around about 21%. But I know your target is 20%. But I think the ultimate question is, is that basically, can Critical be a 21-22% margin business over time? Is that a feel of what you feel can be achieved?

Roy Twite: I mean, Jackie is now listening. He's probably going to kill me, Jonathan. I mean, it depends on the cycle as well, right? You need a bit of help from the markets, but we're not putting a lid on margins, as I've said on previous calls, right? And as Aftermarket strength continues, as it delivers the complexity reduction, of course, and if the markets are good, of course, margins can go up 20%+, there's no doubt. And we – as I said, we will continue to invest in the businesses for growth. And I don't want anybody to think that we're not going to be doing that. We're certainly going to be doing that. So, that will obviously constrain margins in the short term slightly. But can we do 21-22%, you certainly couldn't rule it out, Jonathan.

Jonathan Hurn: Okay. So basically, Critical is a 20% margin, a 20%+ margin sort of business rather than, I suppose, the 20% target you have out there really.

Roy Twite: Precisely. And I think we've already said that, Jonathan, actually. I think, 20%+ yeah.

Daniel Shook: Yeah.

Jonathan Hurn: And then a third, just a final one, just coming on – well, just carrying on with Critical. I just wonder if you could talk about nuclear. Obviously, there's a lot of refurbishment activity out there. If you look at your orders in FY22, they were sort of plus one. Can we see a sort of a step-up in terms of that activity coming through?

And just, can you talk about the dynamics of nuclear Aftermarket? Is that really high margin for you? Is that maybe your highest margin segment, or is that not the case?

Roy Twite: Yeah. I mean, certainly, it's high margin. I mean, when we do an upgrade valve in nuclear, which is obviously Aftermarket, that's good margin. The parts are very good margin, obviously. The issue on nuclear is always New Construction. Because everybody knows that the Aftermarket part stream is good. And you need it to be good because the New Construction margins are competitive, I would say, Jonathan. But on the Aftermarket side, it's good. Yeah. And we do see some potential for nuclear.

Timing is always tricky on nuclear because these projects always take longer, whether they're upgrades or New Construction, as you know, right. And anybody that follows, well, any of the big projects knows that it can take longer. But the US, for instance, is prolonging the life of its nuclear power stations. And I think we'll see more and more of that. I think France is obviously dedicated to nuclear and is, at the moment, talking within the EU about making sure that nuclear is counted as a green fuel. And they made some progress on that. They're still obviously talking with Germany about that.

But I think – so for us, yeah, we see nuclear upgrades as profitable. We see the parts as very profitable, and we do, yeah, see some good opportunity there.

Jonathan Hurn: Great, guys. That's very clear. Thank you very much.

Roy Twite: Great. Thanks, Jonathan.

Operator: Thank you. As a reminder, if you would like to ask a question, please press star followed by one on your telephone keypad. And our next question goes to Aurelio Calderon of Morgan Stanley. Aurelio, please go ahead, your line is open.

Aurelio Calderon Tejedor (Morgan Stanley): Hi, good morning. Thanks for taking my questions – I've got two. The first one is on Hydronic. And historically, if we look at the division, it's been more – and correct me if I'm wrong, but it's been more of a balance between growth and margins. I think now, for the first time in several years, we can talk about renovation, we can talk about a structural or a secular kind of uptick in that business. So, how do you think about the margin profile going forward? Is it a matter of growth versus margins, or can you get both in the cycle?

Roy Twite: Yeah. I mean, I think Hydronic, I think since 2019 has grown about 5%, I think, despite COVID and everything else that's hit us. So, I think Phil and team doing a fantastic job. I also think, Aurelio, externally, energy savings definitely come up the agenda, right, for lots of reasons. One is it's got a lot more expensive – energy. Secondly, because of commitments. Carbon commitments by big companies by governments, right?

So, I think to me, it's in a really good place versus where it was three years ago. And as we look forward, I think energy carbon saving is going to stay fundamentally important. As I said in the presentation, the German government is doing faster legislation around energy saving. For instance, I think 80-90% of that business is Europe as well. And the business – the culture in the business is fantastic. They actually got our highest employee engagement scores in the Group, which is great. And what we do, cost to customer, about 2% or 3% of the cost of their HVAC system, but it can save them one-third of the energy cost, right? Because we help them design the system. We help them actually sometimes reduce the

number of pumps in the system. We certainly help them with the way that the whole system is balanced and require less pumping cost.

So yeah, I feel like that business is in a good place. And as we said at the Capital Markets Day, we expect, sort of, 5% growth long-term plus, and we expect 20% margins. And that was before we acquired Heatmiser, which gives us another 100 basis points. And again, I'm not trying to constrain the margins. They'll go 20%+. But we are committed to fully investing in that business, again, to help it grow faster, Aurelio. So yeah. Yeah, I think it's in a good place, that business. And the outlook is healthy. I think mid-single-digit growth again this year, margin improvement again this year. So yeah, we feel good.

Aurelio Calderon Tejedor: That's super helpful. And the second question, I'm sorry to labour the point on Critical margins, but I think it's one of the key highlights in my view. I guess, if we go back to 2021 at your Capital Markets Day, you were talking about kind of 20% to 30% of the Critical business that didn't have margins that were attractive to you. I guess the question is more on, kind of, M&A strategy going forward, especially for Critical. Can we – one is, do we see any obvious parts of the portfolio that need to be taken care of? And second part would be, can we find a Heatmiser for Critical?

Roy Twite: What a brilliant question, Aurelio. That is brilliant. You know what, it's almost like you were listening to a conversation with Jackie, in one of our business meetings. Because we would – obviously, Aftermarket is going great, right? But if we could even take it to the next level, it will probably be via instrumentation, digital, exactly as you say, right, the Heatmiser equivalent.

So, we would love an acquisition like that to accelerate our progress in Critical Aftermarket. Yeah, fantastic.

So, as we think about Critical, the 30% that we had under review, I think you know, I mean, the margins are barely dilutive now on that 30%. And that's a testament to those teams, and to Jackie. Because what they had to do was absolutely flip to get much more Aftermarket business, and they've done that. I mean, and I visited both of the major parts of that business in the last six months. And the teams are great, right? They're focused on refurb. They're focused on driving upgrade valve, just like we've done in the rest of Critical. So, I'm really excited about the prospects for that part of the business.

But acquisitions, as you say, would tend to be more instrumentation and certainly more at driving Aftermarket for the long term, that sort of growth.

Aurelio Calderon Tejedor: That's very helpful. Thank you.

Roy Twite: Thank you.

Operator: Thank you. And our final question goes to Mark Davies Jones of Stifel. Mark, please go ahead, your line is open.

Mark Davies Jones (Stifel): Thank you very much. Morning, both. A couple, if I may, both on Precision, on some of the moving parts there. Firstly, on CV, what's the view for 2023?

Obviously, China was very weak last year should be reopening, getting better. But conversely, supply chain is still very tight. Western cyclical markets a bit weaker. So, how does that balance out, do you think this year?

Roy Twite: Yeah. Mark, I think you just described it perfectly. It's exactly how we see it. We should get a rebound from China. Western markets, we think, well, let's say, flat to slightly down is where we got it. So, we've got the whole thing at flat to slightly down within our 111p. Again, let's hope that things improve from there, but that's exactly how we called it.

Mark Davies Jones: Okay. Great. The other bit was Life Sciences, about which you are sounding quite excited, and clearly Adaptas is going very well. Can that become a much more material bit of the division? And if so, they're fairly niche businesses, do you need to enter more niches? Is that a big focus of M&A?

Roy Twite: Yeah. I think, I mean, certainly, we can grow Life Sciences further, yeah. There's some good opportunities, and Beth, Martin and the team are doing a cracking job. And I think the talent in that team and the opportunities they're opening up – and Beth told me about another couple of contracts that we won by the Adaptas team. So, just literally the other day, Mark. So, I feel really good about Life Sciences, yes, the funnel is good in terms of opportunity.

We're trying to do more of what we did with Heatmiser. Well, we did it with CorSolutions. I know it's a lot smaller. But yes, they tend to be quite niche, technically very, very capable. And what we look for is, obviously, acquisitions that have already established good product market fit. We obviously check with the customers. We know most of those customers pretty well now, that it's a technology or a product that's really going to get some traction. So, it does take a bit of time. It is a very selective process, but the funnel has got some interesting opportunities in it, yeah.

Mark Davies Jones: Presumably, that part of the Precision portfolio should be still growing nicely in 2023 given the backdrop.

Roy Twite: Absolutely. Absolutely, Mark, yeah.

Mark Davies Jones: We're past all the valve surge stuff now, so that falls out of the comp.

Daniel Shook: Yeah, that's out of it.

Roy Twite: Yeah. As you saw the underlying, you know, that grew about 10% last year, and yes, we're past all the ventilator valve stuff.

Having said that, we've actually had an order in January to support China on ventilators, quite a large one. So yes, I mean, in terms of the real noise, you know, the big stuff, I think we're past it, yeah.

Daniel Shook: Yeah.

Mark Davies Jones: Great. Thanks very much.

Roy Twite: Great. Thanks, Mark.

Daniel Shook: Thanks, Mark.

Operator: Thank you. We have no further questions. I'll hand back to Roy for any closing remarks.

Roy Twite: Brilliant. I think from my perspective, it's a good, solid set of results. The strategy that we announced back in 2019 is clearly working really well. Customer satisfaction is high, employee engagement is high. We've added, as I said, almost £100 million to profit

since 2019. I think we've got great momentum in this business. And actually, as we sit here today, we feel reasonably optimistic about this year.

So, thanks for joining us, everybody, and all the best. Thank you.

[END OF TRANSCRIPT]