MACFARLANE GROUP

2018 Results

Overview

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- Business Review
  - Packaging Distribution
  - Manufacturing Operations
- Pension Scheme Deficit
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- Conclusions

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Executive Summary

Profit before Exceptional Items	**2018**	2017
	£11.2m	£9.3m

- Group sales £217m, 11% growth on 2017
- Profit before exceptional items £11.2m, 20% growth on 2017
- Distribution sales growth 11% of which 4% organic, 7% acquisition
- Distribution profit growth of 18%
- Manufacturing Operations sales growth 13%, profits up 31%
- Pension deficit has reduced by £2.0m to £9.8m
- Net bank debt £13.2m, down £1.1m in in 2018
- Two further acquisitions within Packaging Distribution
- Final dividend increased by 10% to 1.65p per share payable 06-Jun-19, with a register date 17-May-19

Financial Summary – 2018

Revenue and profit	Revenue ▲ 11%	Profit before exceptionals ▲ 20%	EBITDA ▲ 19%
Returns and balance sheet	Pre-tax ROCE ► 19%	Bank debt ▼ £13.2m	Pension deficit ▼ £9.8m
EPS and dividend	Diluted EPS ▲ 9%	EPS before exceptionals ▲ 5.72p	Dividend per share ▲ 2.30p

Results £m

	2018		2017		2016	
Sales		**217.3**		196.0		***179.8***
Gross Profit	**30.6%**	**66.5**	30.8%	60.3	***31.0%***	***55.7***
Overheads exc. DA		**50.7**		47.2		***44.6***
EBITDA		**15.8**		13.1		***11.1***
Depreciation/amortisation		**3.8**		3.0		***2.4***
Operating profit		**12.0**		10.1		***8.7***
Interest		**0.8**		0.8		***0.9***
Profit before exceptionals		**11.2**		9.3		***7.8***
Diluted EPS	**5.72p**		5.22p		***4.64p***	
Dividend	**2.30p**		2.10p		***1.95p***	
Dividend cover	**2.5**		2.5		***2.4***	

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Cash Flow £m

	2018	2017	***2016***
EBIT	**11.7**	10.1	***8.7***
DA	**3.8**	3.0	***2.4***
EBITDA	**15.5**	13.1	***11.1***
Working Capital	**1.4**	(0.8)	***(3.2)***
Interest	**(0.5)**	(0.5)	***(0.5)***
Acquisitions	**(5.6)**	(8.3)	***(8.7)***
Share placing	**-**	7.6	***5.6***
Tax	**(1.9)**	(1.9)	***(1.3)***
Capital expenditure	**(1.4)**	(1.7)	***(1.1)***
Pension	**(2.7)**	(3.3)	***(2.9)***
Dividend	**(3.4)**	(2.8)	***(2.3)***
Movement in debt	**1.4**	1.4	***(3.3)***

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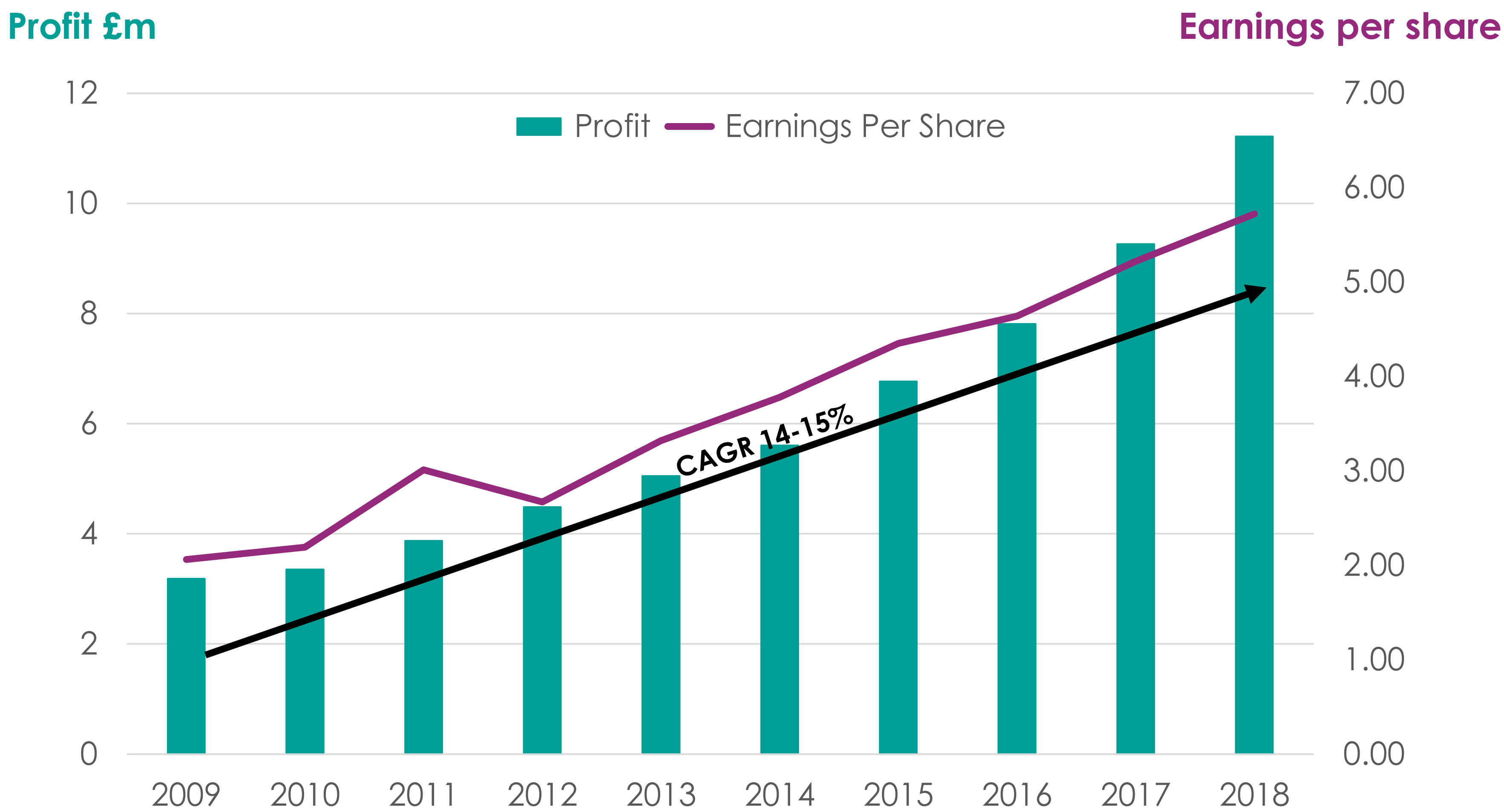
Profit Progression

Profit before tax



Packaging Distribution

£m	2018	2017
Revenue	**189.8**	171.8
Gross margin	**56.0**	50.4
Overheads	**44.8**	41.0
Operating profit	**11.2**	9.4
OP Margin	**5.9%**	5.5%

- Sales increase 11%, 4% organic and 7% acquisition
- Sales split 72% Industrial 28% Retail
- Gross margin 29.5%, (2017: 29.3%) reflects acquisition benefits and recovery of corrugated increases Q2
- Majority of overhead increase is acquisition-related
- Net promoter score 46 (2017: 48)

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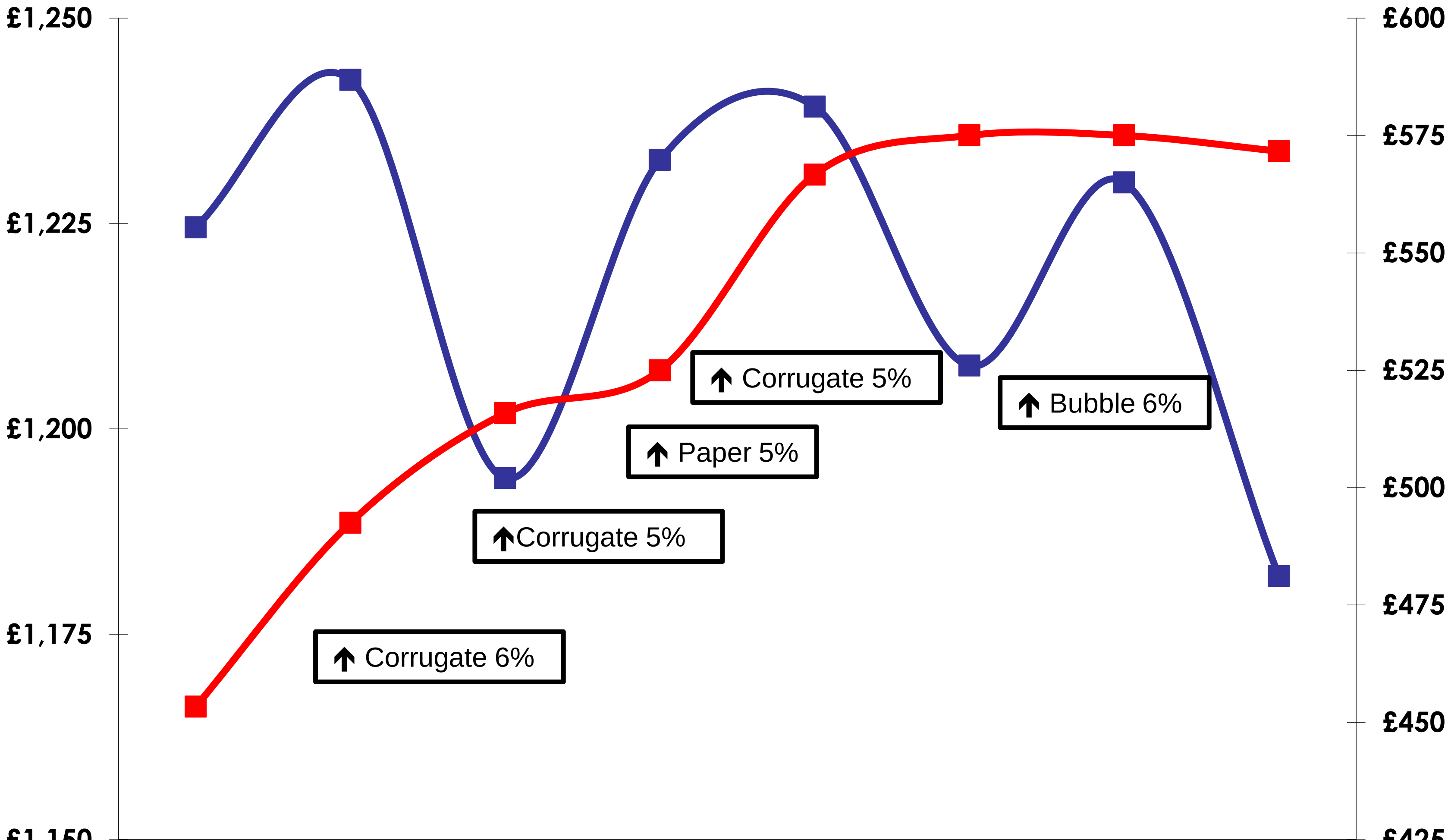
Packaging Distribution – Raw Material Movements



	Q1 2017	Q2 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018	Q3 2018	Q4 2018
Polymer £/tonne	£1,225	£1,242	£1,194	£1,233	£1,239	£1,208	£1,230	£1,182
Paper £/tonne	£453	£493	£516	£525	£567	£575	£575	£572

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Packaging Distribution

- Revenue increases in H1 through internet retail upspend from Dixons/Carphone £0.4m, Urbn £0.3m and Ocado £0.2m – Retail sector closed softly in Q4
- Internet retail ca. 21% of Distribution revenue
- National Accounts growth up significantly with strong increase from Rittal £0.8m, Keter £0.7m, Corbus £0.4m and Thermofisher £0.4m
- Acquisitions both performing well
- Further acquisitions being targeted
- New business wins in 2018 – Body Shop, Dunelm and Urbn Outfitters
- Discussions advanced with a number of existing customers to provide them with a European service

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Packaging Distribution – Acquisitions 2014 to 2018

Acquisition	Location	Sales	EBITDA multiple	Placing price	Integrated
Lane Packaging	Reading	£3m	5-6 x	N/A	✓
Network Packaging	Wolverhampton	£9m	5-6 x	Sep-14 **37.5p**	Q1 2019
OnePackaging	Bingham	£5m	5 x	N/A	✓
Colton Packaging Teesside	Teesside	£3m	5 x	N/A	✓
Edward McNeil Ltd	Glasgow	£3m	5 x	N/A	✓
Nelsons for Cartons & Packaging	Leicester	£9m	5-6 x	Jul-16 **58.0p**	TBD
www.boxesdirect.co.uk	Nottingham	£15m	5 x	Sep-17 **66.0p**	H2 2020
Tyler Packaging Leicester Ltd	Leicester	£2.5m	5 x	N/A	Q2 2019
Harrison's Packaging Ltd	Leyland	£3.5m	5 x	N/A	TBD

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Macfarlane Design and Manufacture

£m	2018	2017
Revenue	**13.9**	12.3
Gross Margin	**35.5%**	36.0%
Operating profit	**0.4**	0.2
Sales to Distribution	**22%**	23%

- Strong sales demand from exporters
- Operational changes implemented to reduce costs and improve manufacturing workflows when absorbing new business wins
- Strong new business pipeline for 2019
- Focus on value-added products

Macfarlane Labels

£m	2018	2017
Revenue	**18.3**	15.9
Gross margin	**33.1%**	37.7%
Operating Profit	**0.5**	0.5
Self-Ad/Reseal-it %	**50/50**	53/47

- Re-sealable labels sales/machines up 24%
- Self-adhesive label sales up 7%
- Investment in new printers to increase exports and improve margin
- Gross margin impacted by continuing highly competitive UK retail environment
- Reorganised Kilmarnock operation £0.1m cost

Pension Scheme Deficit £m

	2018	2017
Opening deficit	**(11.8)**	(14.5)
Ongoing accrual/Interest cost	**(0.4)**	(0.5)
GMP equalisation – exceptional items	**(0.3)**	-
Contributions	**2.8**	3.4
Bond yield ↑ 0.3% to 2.8% (2017 ↓ 0.2%)	**4.1**	(2.9)
Investment returns	**(4.1)**	3.7
Net effect of other assumptions	**(0.1)**	(1.0)
Closing deficit	**(9.8)**	(11.8)

- GMP equalisation for all schemes – lesser impact in our scheme
- Continued increase in bond yields helps but offset by LDIs; however
- LDI provided ca. 80% hedge vs. interest liabilities
- Transfer values continue to be a key feature
- Deficit recovery contributions for 2019 £3.0m (inc. ongoing costs £0.4m)
- Next actuarial valuation 1-May-20

Pension Scheme Details £m

Investments		**H1 2018**	2017
Growth assets	Disinvested		
Diversified Growth Funds	£3.1m	**17.5**	21.5
Equities		**16.0**	17.7
European Loan Fund		**6.6**	6.6
Long-term Property Fund		**7.1**	6.6
Matching assets			
Liability-driven Investments		**28.4**	28.5
Cash		**0.2**	0.1
Total investments		**75.8**	81.0
Liabilities	Members		
Active members	**16** (17)	**5.0**	5.0
Deferred members	**216** (241)	**29.5**	34.3
Pensioners	**358** (347)	**51.1**	53.5
Total liabilities	**590** (605)	**85.6**	92.8

Profitable Growth in Packaging Distribution

Growth	Proposition	Capability
Retail	Reduce total cost of packaging	Expertise, 3PL partnerships and customer referrals
Industrial	Rationalise packaging supplier base to reduce costs	UK national network IT capability
Geographic expansion	Rationalise packaging supplier base to reduce costs	"Follow the Customer" programme
Acquisition	Regional infill leveraging existing network	Experience and case studies

Performance Improvement	Proposition	Capability
Sourcing	Reduce input prices	Leverage scale Strategic supplier base
Operations	Reduce property costs Reduce cost to serve	Streamline property footprint Logistics best practice

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Profitable Growth in Manufacturing

Growth	Proposition	Capability
Aerospace, Medical, Electronics	Unique protection for high value, fragile Items	Leading-edge MOD approved Design, expertise
Re-sealable Labels	Ease of opening, food waste reduction and brand integrity	Proven Patented technology

Performance Improvement	Proposition	Capability
Commercial Approach	Margin protection against volatile ordering patterns	Activity-based pricing
Operations	Improved operational efficiency	Selective investment and best practice focus

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Brexit impact

- Risk assessment commenced in 2018
- Concentration on potential impact of "No-deal" Brexit
- Principal areas of impact

  Maintain robust supply chain for customers given 10% purchases from Europe and 5% from Rest of the World
  Currency fluctuations - Euro purchases 6m Dollar purchases $2.1m
  Higher tariffs under WTO rules – knowledge of customs processes
  Labour risk – 33 staff are EU nationals

- Impact and response

  Potential stock build in March 2019 of £500k of product
  Stock build in Germany for specific customers
  1% movement in currency costs £50k – effectively price movement
  WTO tariff rates – additional £420k – training requirement for staff
  Support EU staff with documentation / employment confirmations

- We are working with customers, suppliers and staff to provide effective support through a challenging period

Conclusions

- 2018 was another year of continuing progress in line with our strategy
- 2019 has started well
- Trading agenda:
  - Distribution focus on identified growth opportunities – Internet Retail, National Accounts (mainly industrial customers), 3PL and expansion of capability in Europe
  - Manufacturing focus on operational improvements and higher added value products and services
  - Big focus on cost reduction/consolidation/integration initiatives
- Pipeline of further acquisition targets being pursued for 2019
- Balance sheet agenda:
  - Implement additional pension deficit reduction actions
  - Focus on cash generation
- Bank facilities in place until June 2022 to support growth plans

Macfarlane Business Case

A simple and flexible business model

Strong operating companies with differentiated propositions

Good market positions with growth potential

Clear plans and a track record of performance

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