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View our Annual Report and Accounts and other information about Macfarlane Group at [macfarlanegroup.com](http://macfarlanegroup.com)

## Celebrating 70 years

### 1949

Macfarlane Group founded by Lord Macfarlane of Bearsden KT



### 1973

Floated on the London Stock Exchange

### 1980

Acquired Abbott's Packaging

### 1983

Accredited ISO9001



### 2001

Acquired National Packaging

### 2005

Launched Customer Connect and Online Ordering



### 2007

Accredited ISO14001

### 2014-19

11 acquisitions including Network Packaging, Nelsons for Cartons & Packaging and Greenwoods Stock Boxes



### 2016

Opened Innovation Lab



### 2019

Macfarlane Group celebrates its 70th anniversary





## Financial and operational highlights 2019



**£225m**

Sales

**6.0%**

Operating profit  
(as % of sales)

**£12.0m**

Profit before tax

**6.5%**

Dividend increase

**>250,000**

Annual deliveries

**>1,700**

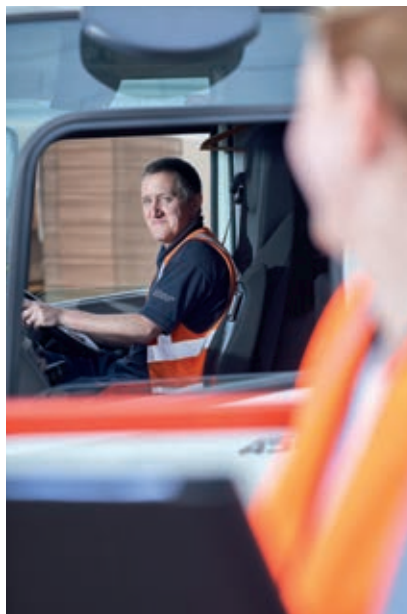
Bespoke designs

## Macfarlane Group – serving our customers

Headquartered in Glasgow, Macfarlane Group PLC employs over 925 people at 33 sites in the UK, one in Ireland and one in Sweden and services more than 20,000 customers in a wide range of sectors.

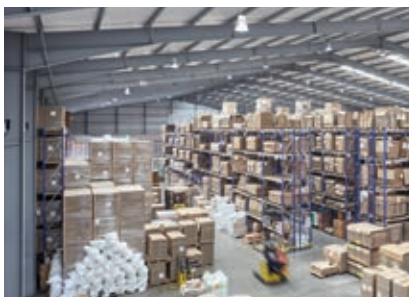
### North \*

Sales: **£73.0m**  
 No. of employees: **239**  
 No. of vehicles: **37**  
 No. of sites: **10**  
 No. of customers: **4,377**



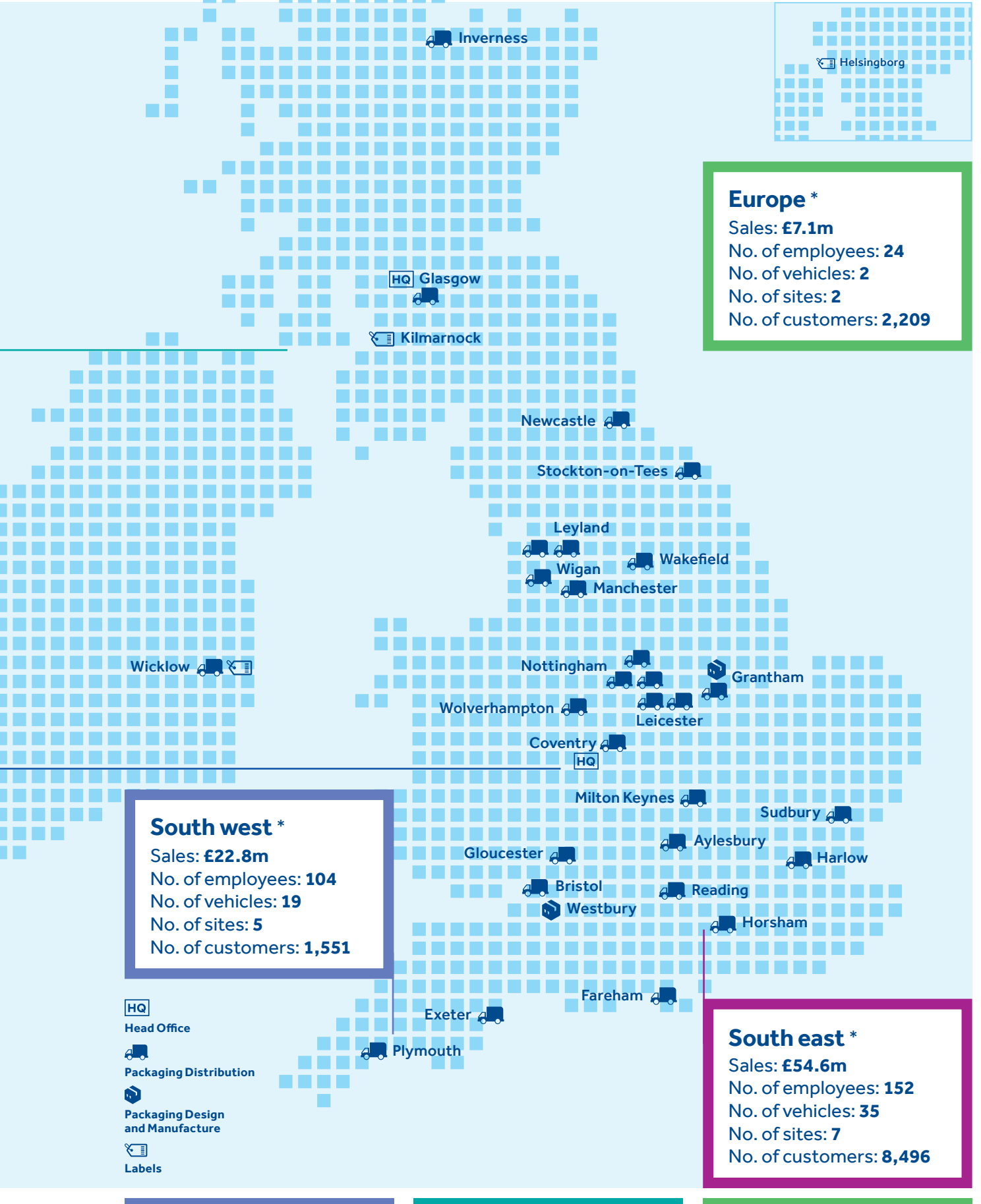
### Midlands \*

Sales: **£67.9m**  
 No. of employees: **286**  
 No. of vehicles: **47**  
 No. of sites: **9**  
 No. of customers: **3,420**



\* Numbers relate to operating sites only





## Chairman's statement

Macfarlane Group PLC achieved sales of £225.4 million in 2019, (2018: £217.3 million) a 4% increase on 2018, with 2019 profit before tax growing to £12.0 million (2018: £10.9 million), 10% ahead of 2018. This marks the tenth consecutive year of profit growth.

The performance in 2019 was in line with market expectations and was achieved against a well-publicised backdrop of economic uncertainty resulting in weaker demand.

### Trading

Packaging Distribution increased sales by 4% in 2019 to £196.7 million (2018: £189.8 million). Sales revenue from existing customers was impacted by both weaker demand and sales price deflation during 2019 but this was offset by good growth in new business and the benefit of £5.7 million from acquisitions. The 2019 acquisitions of Ecopac (U.K.) Limited ('Ecopac') and Leyland Packaging Company (Lancs) Limited ('Leyland') have both performed well since acquisition. Gross margin in Packaging Distribution at 31.1% showed improvement on the prior year (2018: 29.5%) and reflected effective management of input price movements. The growth in sales and gross margin, combined with good cost control, resulted in Packaging Distribution achieving an 11% increase in operating profit before exceptional items to £12.4 million (2018: £11.2 million) after the impact of IFRS 16 'Leases'.

Sales in Manufacturing Operations at £28.7 million (2018: £27.5 million) grew by 4% on the previous year. Gross margin was 38.2% in 2019 compared to 38.4% in 2018. Operating profit before exceptional items in 2019 increased to £1.2 million (2018: £0.8 million) after the impact of IFRS 16 'Leases'.

After net finance costs of £1.6 million (2018: £0.8 million), Group profit before tax totalled £12.0 million, an increase of 10% on 2018. Basic and diluted earnings per share for 2019 were 6.17p (2018: 5.55p) and 6.16p (2018: 5.55p) respectively.

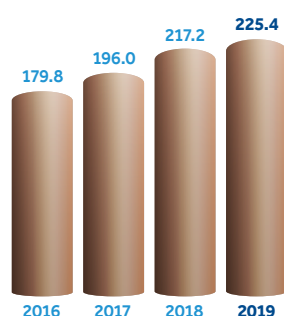
### IFRS 16 'Leases'

IFRS 16 'Leases' requires the Group to recognise right-of-use assets and lease liabilities on the balance sheet and depreciation on the assets and interest on the lease liabilities in the income statement. Previously, operating leases were off balance sheet and leasing costs were reported in overheads. IFRS 16 has been applied from 1 January 2019, with no requirement to restate comparative figures. Whilst there was no major impact on profit before tax, net assets or cash flows from

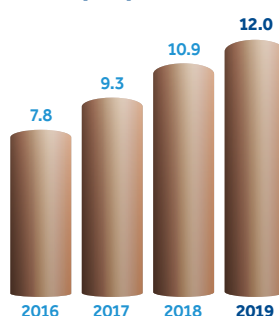


## Group performance

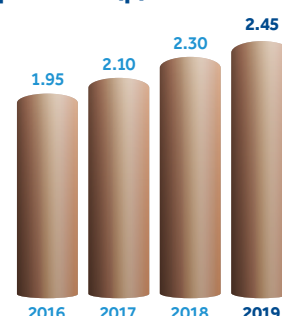
### Sales (£m)



### Profit before tax (£m)



### Dividend per share (p)



applying the standard, there are changes in classifications which are indicated throughout this document.

### Dividend

The Board is proposing a final dividend of 1.76 pence per share, amounting to a full year dividend of 2.45 pence per share, a 7% increase on the prior year's dividend of 2.30 pence per share. Subject to the approval of shareholders at the Annual General Meeting on Tuesday 12 May 2020, this dividend will be paid on Thursday 4 June 2020 to those shareholders on the register at Friday 15 May 2020.

### Net bank debt

The Group's net bank borrowing at 31 December 2019 decreased by £0.5 million to £12.7 million from £13.2 million at the previous year-end. The Group's bank facility of £30.0 million with Lloyds Banking Group is available until June 2022 and accommodates normal working capital requirements as well as supporting acquisition funding.

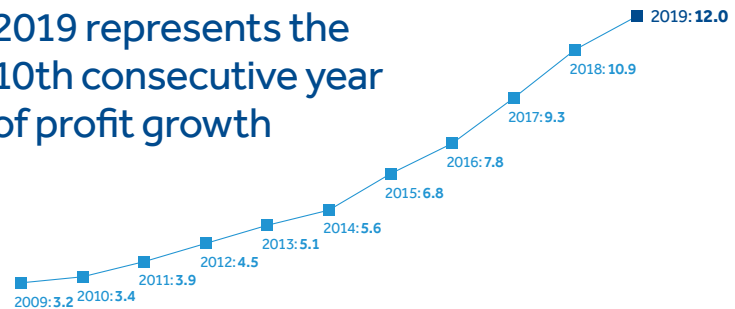
### Pension scheme

The Group's pension deficit at 31 December 2019 decreased by £3.3 million to £6.5 million (2018: £9.8 million). Although the discount rate decreased, which increased the value of the pension liabilities, this was offset by increases in the value of the scheme's holding in liability-driven investments and its other investments.

Following the High Court judgement involving Lloyds Banking Group

## Profit before tax (£m)

2019 represents the 10th consecutive year of profit growth



pension schemes on 26 October 2018, a charge of £0.3 million was made in 2018 as an exceptional item. This represented past service cost in respect of the equalisation of Guaranteed Minimum Pensions ('GMP') benefits between 1990 and 1997. When we refer to items before exceptional items, it excludes these charges, which we believe provides a more meaningful basis for measuring our financial performance in 2018.

### Outlook

Continued profit growth over a ten year period confirms the Board's confidence that its consistent strategy of positioning the business to serve key growth markets in the protective packaging sector remains appropriate and continues to be effective.

2020 has started well and profitability in the year to date is ahead of the same period in 2019.

The business will remain focused on the delivery of continued profit growth through the provision for our customers of added-value protective packaging products and services in target market sectors, combined with efficiency improvements and the completion of value-enhancing acquisitions. We will also focus on ensuring that we support our customers in achievement of their sustainability objectives.

Macfarlane Group's performance in 2019 reflects the successful implementation of our strategy and we are confident that the Group will deliver further progress in 2020.

**Stuart R. Paterson**  
Chairman  
27 February 2020

## Macfarlane investment case



## Business model and strategy

### Our business model

We design, manufacture and distribute protective packaging products and labels to business users. Protective packaging products are mainly sold to customers in the UK. Labels are sold to customers in the UK, mainland Europe and the USA. For reporting purposes, we split the Group into two segments:

- Macfarlane Packaging Distribution; and
- Manufacturing Operations, comprising Macfarlane Design and Manufacture and Macfarlane Labels.

The Group operates a Stock and Serve model from 25 Regional Distribution Centres (RDCs) providing a UK national network to support customers on a local, regional and national basis and 3 satellite sites linked to RDCs. In addition the Group also operates four manufacturing centres, two in Design and Manufacture and two in Labels. There is a central administration centre in Coventry, a Labels design centre in Sweden and the Group head office is located in Glasgow.

Macfarlane Group has over 925 employees, mainly in the UK but also in Sweden and Ireland. Our sites range in size from over 100 employees at manufacturing locations to under 20 for smaller RDCs and satellite sites. The Group operates a decentralised structure for sales and operations supported by central functional teams covering key areas such as procurement, logistics, HR, IT and finance.

### How our business generates value

Macfarlane is the UK market leader in the distribution of protective packaging products. Macfarlane leverages its purchasing scale to cost-effectively source a comprehensive range of protective packaging products and adds value for the customer by providing independent advice on the most cost-effective choice of product and packing processes, and operating as a single-source supplier for these products on a Just In Time basis with tailored stock management programmes and electronic trading capability.

The manufacturing businesses utilise design, intellectual property and know-how to provide a bespoke service to support major manufacturing customers to cost-effectively protect their high-value products in storage and distribution and for FMCG customers to attractively display and accurately identify their products at the point of sale.

Macfarlane aims to grow its business by increasing the penetration of existing customers and winning new customers.

There will be a natural churn of packaging requirements from our existing customers and we experience a level of sales erosion each year as we optimise protective packaging solutions for customers. Therefore new business generation is key to Macfarlane Group's overall growth and there is specific measurement and focus on this area.



## Our strategy

For many years we have followed a consistent strategy to create value for shareholders. We seek to operate in markets which give above-average growth opportunities to develop business with existing customers and generate business with new customers.

At the same time we seek to improve the performance of the business by more effective sourcing and increasing the efficiency of our logistics and property portfolio. We then supplement this growth in the existing business by acquiring quality businesses. The Group objective is to grow sales volumes and achieve a pre-tax return on sales of between 5% and 7%. We are now achieving returns in that target range. The following table summarises the key strategic priorities.

### Strategic priority 1

We seek to implement a segmental sales strategy to improve customer retention levels, increase product penetration and accelerate new business, and focus on key sectors with above average growth potential, particularly National Accounts and internet retail.

#### 2019 progress

- Continuing this approach has provided increased customer focus.
- New business growth in Packaging Distribution increased by 11% from 2018 to 2019.
- Our Innovation Lab continues to prove an effective tool to demonstrate the range of our capability to customers.
- Net promoter score increased to 50 (2018: 46) reflecting the success of our strategy.

### Strategic priority 2

We work to enhance gross margins through a focus on higher added value products and more effective sourcing.

#### 2019 progress

- Both strategic and tactical purchasing programmes are in place to improve our sourcing capability in Packaging Distribution.
- Gross margins within Manufacturing Operations have increased during the year as we resolved operational issues.

### Strategic priority 3

We ensure operational effectiveness is maximised through efficiencies in our logistics operations.

#### 2019 progress

- Logistics costs reduced to 2.5% of sales (2018: 2.6%) through use of the Paragon planning tool and driver training.

### Strategic priority 4

We seek to optimise the costs associated with the physical infrastructure of our business.

#### 2019 progress

- Property costs increased to 4.3% of sales (2018: 3.9%) reflecting additional costs in 2019 in our property network. Our aim is to reduce the levels of costs below 4.0% of sales in 2020.

### Strategic priority 5

We aim to supplement organic growth with at least two good quality acquisitions each year.

#### 2019 progress

- We completed the acquisition of Ecopac on 2 May 2019 and Leyland on 30 August 2019.

## Chief Executive's review – Packaging Distribution

Macfarlane Packaging Distribution is the leading UK specialist distributor of protective packaging materials. Macfarlane operates a Stock and Serve supply model from 25 Regional Distribution Centres (RDCs) and 3 satellite sites, supplying industrial and retail customers with a comprehensive range of protective packaging materials on a local, regional and national basis.

Competition in the packaging distribution market is from local and regional protective packaging specialist companies as well as national/international distribution generalists who supply a range of products, including protective packaging materials. Macfarlane competes effectively on a local basis through its strong focus on and regular monitoring of customer service, its breadth and depth of product offer and through the recruitment and retention of high-quality staff with good local market knowledge. On a national basis Macfarlane has focus, expertise and a breadth of product and service knowledge, all of which enables it to compete effectively against non-specialist packaging distributors.

Macfarlane benefits its customers by enabling them to ensure their products are cost-effectively protected in transit and storage through the supply of a comprehensive product range, single source Stock and Serve supply, Just In Time delivery, tailored stock management programmes, electronic trading and independent

### Packaging Distribution

	Base business £000	Impact of 2019 acquisitions £000	2019 £000	2018 £000	2019 growth
Revenue	190,976	5,730	<b>196,706</b>	189,835	<b>3.6%</b>
Cost of sales			<b>(135,525)</b>	(133,843)	
Gross margin			<b>61,181</b>	55,992	<b>9.3%</b>
Operating expenses (recurring)			<b>(48,775)</b>	(44,820)	<b>8.8%</b>
Operating profit before exceptional item	11,771	635	<b>12,406</b>	11,172	<b>11.0%</b>
Operating expenses (exceptional)			–	(270)	
Operating profit			<b>12,406</b>	10,902	<b>13.8%</b>

advice on both packaging materials and packing processes.

#### 2019 trading

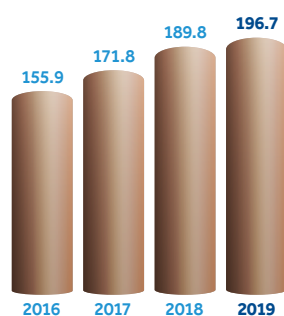
Macfarlane Packaging Distribution grew sales by 3.6% in 2019. Whilst existing business was impacted by weaker demand conditions and sales price deflation, this was partly compensated for by good new business growth, 11% ahead of levels achieved in 2018. Gross margin in Packaging Distribution was 31.1%, (2018: 29.5%) with the

improvement demonstrating our ability to effectively manage input price changes on paper-based products with our customers.

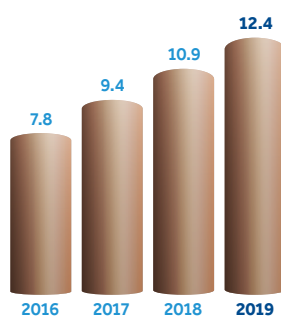
We also continued to deliver the benefit from acquiring high quality packaging distribution businesses – the acquisitions of Ecopac at the start of May 2019 and Leyland at the end of August 2019 both performed well and we benefited from a full year contribution from the 2018 acquisitions.

### Packaging Distribution performance

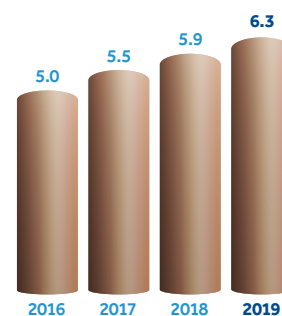
#### Sales (£m)



#### Operating profit (£m)



#### Return on sales (%)







Macfarlane operates a Stock and Serve supply model from 25 RDCs and three satellite sites.

During 2019 we continued to make steady progress in extending our service into Europe to support a number of our pan-European customers. We also successfully transitioned our business in London from a high cost site in Enfield to a new lower cost facility in Harlow, supported by additional space in Sudbury.

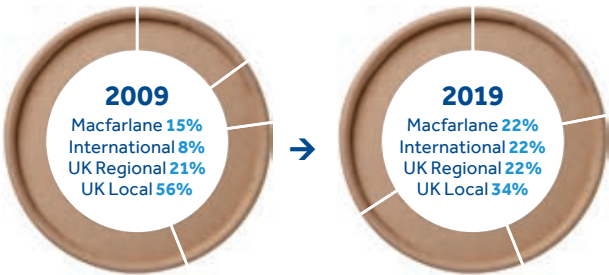
Cost control remained strong and operating profit for Packaging Distribution at £12.4 million grew 13.8% versus 2018, representing a return on sales of 6.3% (2018: 5.9%).

Future plans

2020 plans are focused on continuing to grow sales and improving profitability by the following actions:

- Prioritising our sales activity on the growth potential for protective packaging in key markets – National Accounts in the industrial sector, the e-commerce sector in the retail space and Third Party Logistics ('3PL') operators;
- Demonstrating our ability to add value for customers through further development of our 'Significant Six' sales approach to reduce their 'Total Cost of Packaging' and support their sustainability objectives;
- Continuing to effectively manage the impact of input price changes on paper-based products;
- Rolling out our new web-based solutions to allow customers access to our full range of products and services;
- Accelerating our 'Follow the Customer' programme in Europe;
- Improving our sourcing through strengthening our relationships with key strategic suppliers;
- Implementing further operational savings in logistics by expanding the use of the Paragon vehicle management system and extending our warehouse best practice programme;
- Reducing operating costs by consolidating our property footprint;
- Maintaining the focus on working capital management to facilitate future growth; and
- Supplementing organic growth through completion of further suitable quality acquisitions.

UK Packaging Distribution  
UK market – recent development



Macfarlane customers



## Chief Executive's review – Manufacturing Operations

Manufacturing Operations comprises our Packaging Design and Manufacture business and our Labels business.

The principal activity of the Packaging Design and Manufacture business is the design, manufacture and assembly of custom-designed packaging solutions for customers requiring cost-effective methods of protecting high value products in storage and transit. The primary raw materials are corrugate, timber and foam. The business operates from two manufacturing sites in Grantham and Westbury, supplying both directly to customers and also through the RDC network of the Packaging Distribution business.

Key market sectors are defence, aerospace, medical equipment, electronics and automotive. The markets in which we operate are highly fragmented with a range of locally based competitors. We differentiate our market offering through technical expertise, design capability, industry accreditations and national coverage through the Packaging Distribution business.

Our Labels business designs and prints self-adhesive labels for major Fast-moving Consumer Goods ('FMCG') customers in the UK and Europe and resealable labels for major customers in the UK, Europe

### Manufacturing Operations

	2019 £000	2018 £000
Revenue	<b>28,683</b>	27,455
Cost of sales	<b>(17,731)</b>	(16,906)
Gross margin	<b>10,952</b>	10,549
Operating expenses (recurring)	<b>(9,728)</b>	(9,696)
Operating profit before exceptional item	<b>1,224</b>	853
Operating expenses (exceptional)	<b>–</b>	(60)
Operating profit	<b>1,224</b>	793

and the USA. The business operates from production sites in Kilmarnock and Wicklow and a sales and design office in Sweden, which focuses on the development and growth of our resealable labels business, Reseal-it.

The Labels business has a high level of dependence on a small number of major customers. Management works closely with these key customers to ensure high levels of service and to introduce product and service development initiatives to achieve competitive differentiation.

#### 2019 trading

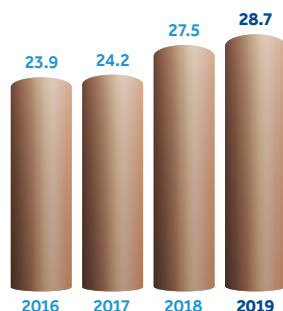
2019 sales for Packaging Design and Manufacture were 2% below 2018 due to demand weakness

particularly in the automotive sector. However actions to improve operational performance and margins resulted in profitability in 2019 being well above that in 2018. Our sales team has continued to develop a strong pipeline of new customer relationships, which should benefit the business in 2020.

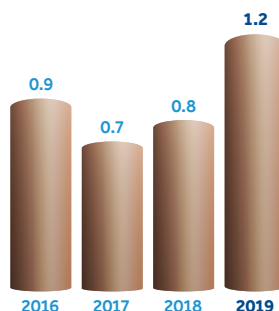
Labels' sales increased by 8% in the year as penetration of our resealable range improved and a number of new business wins were achieved. Despite margin being impacted by the increasingly competitive conditions in the retail sector, profits in the Labels business were similar to 2018.

### Manufacturing Operations performance

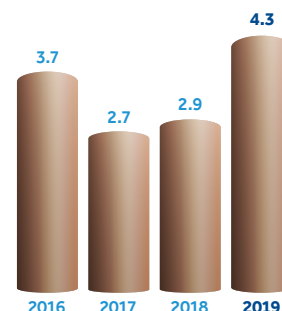
#### Sales (£m)



#### Operating profit (£m)



#### Return on sales (%)







Our Manufacturing Operations design and manufacture a high quality range of bespoke packaging and labelling solutions for our customers.

### Future plans

Priorities for the Manufacturing Operations in 2020 are to:

- Restore Design & Manufacture sales growth in target sectors, Defence, Aerospace and Medical;
- Continue to improve operational efficiency at both Design & Manufacture sites;
- Prioritise new sales activity on our higher added-value bespoke composite pack product range;
- Continue to strengthen the relationship between our Design & Manufacture operations and our Packaging Distribution business to create both sales and cost synergies;
- Accelerate the Reseal-it growth momentum for resealable labels through improved geographic penetration, extending the product range and introducing Reseal-it to new product sectors; and
- Achieve efficiency benefits from recent investments in additional printing capacity and digital printing capability to improve Labels' gross margins.

## Chief Executive's review – 2020 Group outlook

Our sales efforts in 2020 will focus on those segments of the protective packaging market, such as e-commerce, which are forecast to show above average growth rates and those industrial markets where customers recognise the added value brought to their operations by a specialist national protective packaging distributor.

We will continue to add value for customers through our Significant Six sales approach and support them in achieving their sustainability objectives.

In 2020 we plan to acquire further good quality protective packaging businesses, improve our geographic coverage, develop new products introduced by recent acquisitions, work more closely with strategic suppliers and improve operational efficiency by leveraging our property and logistics footprint.

Macfarlane businesses all have strong market positions with differentiated product and service offerings. We have a flexible business model and a clear strategic plan incorporating a range of actions, which are being effectively implemented and reflected in our consistent, profitable growth over a ten-year period.

Our future performance is largely dependent on the successful execution of actions to grow sales, increase efficiencies and bring high-quality acquisitions into the Group. We expect 2020 to be another year of progress for Macfarlane Group.

**Peter D. Atkinson**  
Chief Executive  
27 February 2020

### Five year record

	2019 £000	2018 £000	2017 £000	2016 £000	2015 £000
<b>Turnover</b>	<b>225,389</b>	217,290	195,991	179,772	169,132
<b>Operating profit before exceptional item</b>	<b>13,630</b>	12,025	10,089	8,712	7,702
Net interest payable	(1,606)	(809)	(828)	(901)	(935)
<b>Profit before exceptional item</b>	<b>12,024</b>	11,216	9,261	7,811	6,767
Exceptional item	–	(330)	–	–	–
<b>Profit before tax</b>	<b>12,024</b>	10,886	9,261	7,811	6,767
Taxation	(2,293)	(2,145)	(1,837)	(1,761)	(1,317)
<b>Profit for the financial year</b>	<b>9,731</b>	8,741	7,424	6,050	5,450
<b>Basic earnings per ordinary share</b>	<b>6.17p</b>	5.55p	5.22p	4.64p	4.35p
<b>Dividends</b>	<b>3,689</b>	3,387	2,854	2,358	2,094
<b>Dividends paid per ordinary share</b>	<b>2.34p</b>	2.15p	2.00p	1.84p	1.68p
<b>Dividend cover</b>	<b>2.6</b>	2.6	2.6	2.6	2.6

This table reflects the five-year record for the Group's operations as classified at 31 December 2019.



## Our Innovation Lab

Located in Milton Keynes, the Innovation Lab is a purpose built space to create solutions for the most demanding packaging challenges.

### 1 Significant savings

The ultimate purpose of the Innovation Lab is to optimise pack design and packaging operations and thereby reduce cost throughout the supply chain.

### 2 Cutting edge technology

Our state-of-the-art technology includes interactive touchscreens, digital printers and augmented reality solutions.



### 3 Features and benefits

These can range from customer experience/operational efficiencies, product solutions and general reduction and optimisation outcomes.

### A staged process

The journey begins by understanding the total cost of the customer's packaging process and the business goals. Our team can then explore alternatives with the customer, shortlist preferences, produce a prototype, refine the concept and let the customer leave with a solution.

## Helping our customers benefit from the Significant Six

Our customers' products must arrive in perfect condition, on time, in a cost efficient and sustainable manner.

At Macfarlane Packaging, we have spent decades innovating and perfecting packaging solutions for a wide range of markets that are strong, efficient and sustainable. In doing so, we have isolated six hidden costs that have the biggest impact on most packaging operations... we call these costs 'The Significant Six' and they can account for 90% of all costs in a packaging operation.



# 1.

### Storage costs

With over 700,000 sq ft of warehouse space and a fleet of over 100 vehicles, our nationwide RDCs mean that customers' packaging stock levels can be minimised.

### Industrial customer: Exertis

"As part of the Exertis sustainability focus and through our strategic partnership with Macfarlane, collectively we have identified and removed 18 tonnes of single trip plastic and 45 tonnes of CO<sub>2</sub>e from our UK supply chain for 2020, without compromising quality or security."

Alan Lynch, Global Logistics Director

# 2.

### Productivity costs

We can review the end-to-end customer pack operation to identify space, time and process efficiencies to aid productivity at all stages.

# 3.

### Administration costs

As the UK's biggest packaging supplier we can provide insight to enable our customers to reduce the costs associated with managing multiple suppliers.

4.

### Customer experience

Macfarlane can help enhance the consumer experience of packaging form and brand but at the same time be mindful of cost implications.



### Retail customer: Hobbycraft

"With a thorough approach using innovative ideas in their Innovation Lab and proven methods from their vast experience, Macfarlane have quickly improved the customer journey at Hobbycraft. Macfarlane are very much a partner in our journey for great customer service as much as they are a key stakeholder in finding us the best solutions."

Shabbir Yusoof, General Manager



5.

### Transport costs

By re-thinking the pack design, significant reductions in storage, postal and courier charges can be achieved, whilst improving product protection at the same time.

6.

### Damages and returns

By challenging areas in the customer supply chain where there are damages and returns, we can find the right packaging solution to protect the product and the brand too.



## Finance review

### 2019 represents the Group's tenth consecutive year of growth in its profit before tax.

#### Trading

The Group saw growth in sales of 3.7% during 2019, mainly driven by Packaging Distribution, enhanced by profitable contributions from recent acquisitions. Group sales are £225.4 million, an increase of £8.1 million from 2018. Profit before tax for 2019 increased to £12.0 million, an increase of £1.1 million from that achieved in 2018.

#### Taxation

The tax charge for the year was £2.3 million on profit before tax of £12.0 million, a rate of 19.1%, above the prevailing rate of 19.0% mainly due to acquisition costs not being deductible for tax purposes. This compared with a tax charge of £2.1 million on the profit before tax of £10.9 million in 2018 and a tax rate of 19.7%, above the prevailing rate of 19.0%.

Macfarlane Group and its subsidiary companies have no uncertain tax treatments with HMRC in the UK or with any tax authorities in overseas jurisdictions.

#### Earnings per share

Basic and diluted earnings per share amounted to 6.17p (2018: 5.55p) and 6.16p (2018: 5.55p) respectively, broadly reflective of the increase in profitability. The 2019 calculations take account of the issue of shares in respect of the Leyland acquisition and the dilution caused by the issue of LTIP awards.

#### Dividends

A dividend of 0.69p per share was paid on 10 October 2019. A further dividend of 1.76p per share is subject to approval by shareholders at the AGM in May 2020 and is not included as a liability in these financial statements.

Dividend cover has been maintained at 2.6 times. The Group continues to balance the aim to pay an attractive level of dividend against the need to retain funds in the business to finance growth, make the agreed levels of pension fund deficit contributions, fund acquisitions and meet capital expenditure requirements.

#### Cash flow and net bank debt

The Group's debt facility with Lloyds Banking Group PLC comprises a three-year committed borrowing facility of up to £30.0 million for the period to June 2022, secured over part of Macfarlane Group's trade receivables. The facility bears interest at normal commercial rates and carries standard financial covenants in relation to interest cover and levels of headroom over trade receivables. The Group has been in compliance with these covenants throughout 2019.

The facility accommodates increased working capital requirements from our organic growth as well as finance for pension scheme contributions and an ability to fund acquisitions. Our financing requirements are met through cash generation from profitable trading as well as by maintaining committed borrowing facilities for the medium-term.

The Group had net bank borrowings of £12.7 million at 31 December 2019, a reduction of £0.5 million from the previous year as set out in note 23. The Group's cash generation continued to be strong enabling us to finance growth, make the agreed levels of pension contributions, fund acquisitions and meet capital expenditure requirements. The Group spent £6.3 million on acquisitions in 2019 (2018: £5.6 million) and £2.6 million on capital expenditure in 2019 (2018: £1.5 million).

We will continue to invest where there are needs or opportunities to meet future growth plans. The Group will strive to ensure that in 2020, profit generation is, at the very minimum, matched by cash generation. The Group will remain prudent in its assessment of the likely returns from capital expenditure and potential acquisitions.

#### Acquisitions

On 2 May 2019 the Group's subsidiary, Macfarlane Group UK Limited acquired 100% of the issued share capital of Carnweather Limited (the immediate parent of the trading company Ecopac) for a consideration of approximately £3.9 million. £3.1 million was paid in cash on acquisition, with the deferred consideration of £0.8 million payable in the second quarter of 2020, subject to certain trading targets being met in the year ending 30 April 2020.

On 30 August 2019 the Group acquired 100% of the issued share capital of Leyland for a consideration of approximately £3.05 million. £2.00 million was paid in cash on acquisition with a further £0.25 million met by issuing shares in Macfarlane Group as non-cash consideration. The deferred consideration of £0.8 million is payable in the final quarter of 2020, subject to certain trading targets being met in the year ending 30 August 2020.

Deferred consideration of £1.2 million was paid in 2019 in relation to the 2018 acquisitions of Tyler Packaging (Leicester) Limited and Harrison's Packaging Limited.

### Market capitalisation and share price movements

The number of shares in issue at 31 December 2019 was 157,812,000, reflecting the issue of 264,382 shares on the acquisition of Leyland in August 2019.

At the year-end the Company's market capitalisation was £170.0 million, compared with £112.7 million last year. The share price at 31 December 2019 was 107.75p, compared with 71.50p at 31 December 2018. The range of transaction prices for Macfarlane Group shares during 2019 was 73.00p to 109.00p for each ordinary share of 25p.

### Financial instruments

The Group's principal financial instruments comprise bank borrowings, cash balances and other items, such as trade receivables and trade payables that arise directly from its operations as well as shareholders' equity and deferred consideration arising from acquisitions. The main purpose of these financial instruments is to provide finance for the Group's operations. It is the Group's policy that no speculative trading in financial instruments is undertaken. The main risks arising are liquidity risk and credit risk and the secondary risks are interest rate risk and currency risk. The policies for managing these risks, which have remained unchanged since the beginning of 2019 are set out in note 16 to the financial statements.

### Pension schemes

The Group's pension scheme deficit is sensitive to movements in bond yields, inflation, longevity assumptions and investment returns. The impact of these sensitivities is set out in note 25 to the financial statements.

The Board continues to make regular deficit reduction contributions each year to reduce the deficit. This, combined with careful stewardship of the investment portfolio by the

### Pension scheme deficit

	2019 £000	2018 £000	2017 £000
Fair value of scheme investments	88,061	75,827	80,960
Present value of scheme liabilities	(94,526)	(85,592)	(92,783)
Deficit at 31 December	(6,465)	(9,765)	(11,823)

Trustees, in conjunction with the Group, has helped match the investments with the scheme's liability profile.

Following the triennial actuarial valuation of the scheme at 1 May 2017, the Group agreed a new schedule of contributions with the Pension Scheme Trustees, which assumed a recovery plan period of 7 years. The next triennial actuarial valuation will be carried out at 1 May 2020.

The Group operates a number of defined contribution arrangements for the majority of the employee base. Over 750 of our employees are members of one of these arrangements.

### International Financial Reporting Standards and accounting policies

IFRS 16 'Leases' requires the Group to recognise right-of-use assets and lease liabilities on the balance sheet and charge depreciation on the assets and interest on the lease liabilities in the income statement. Previously, operating leases were off balance sheet and leasing costs were reported in overheads in the income statement. IFRS 16 has been applied from 1 January 2019, with no requirement to restate comparative figures. This has had an effect on the constituent part of the Group's cash flow for the first time in 2019. The cash flow highlights these changes and details of the finance leases and the treatment adopted are set out in the accounting policies note following the financial statements and in note 18.

The Group continues to comply with all International Financial Reporting Standards adopted by the European Union.

### Going concern

The Directors, in their consideration of going concern, have reviewed the Group's cash flow forecasts and profit projections, which are based on the Directors' past experience and their assessment of the current market outlook for the business. The Group's business activities together with the factors likely to affect its future development, performance and financial position are set out in the Chairman's Statement and the Strategic Report on pages 4 to 29.




After making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for at least the next twelve months. For this reason they continue to adopt the going concern basis in preparing the financial statements.

**John Love**  
Finance Director  
27 February 2020

## Principal risks and uncertainties

The principal risks and uncertainties faced by the Group and the factors mitigating these risks are detailed on pages 18 and 19.

These risks are complemented by an overall governance framework including clear and delegated authorities, business performance monitoring and appropriate insurance cover for a wide range of potential risks. There is a dependence on good quality local management, which is supported by an investment in training and development and ongoing performance evaluation.

For highlighted risks shown as   the risk level has remained broadly similar between 2018 and 2019. In respect of the pension scheme which is marked  the risk is considered to have reduced in the year, given the balanced structure of the investment profile and recent changes in mortality tables.

Macfarlane Group has carried out an impact analysis and evaluated the potential short to medium-term implications of a no-deal Brexit including reversion to World Trade Organisation tariffs at 31 December 2020. Where practical, we would put in place contingency measures to try to mitigate any immediate effects on the supply chain. As a business with the majority of its trade in the UK, the principal impact on Macfarlane Group of a no-deal Brexit would be reduced levels of business caused by any significant downturn in the UK economy.

There are a number of other risks that we manage which are not considered key risks. In addition the Group is subject to the impact of general economic conditions including any economic uncertainty, the competitive environment, compliance with legislation and risks associated with business continuity, including cyber-security. These are mitigated in ways common to all businesses and not specific to Macfarlane Group.

### Risk description

#### Raw material prices

The Group's businesses are impacted by commodity-based raw material prices and manufacturer energy costs, with profitability sensitive to supplier price changes including currency fluctuations. The principal components are corrugated paper, polythene films, timber and foam, with changes to paper and oil prices having a direct impact on the price we pay to our suppliers.

#### Property

Given the multi-site nature of its business, the Group has a property portfolio comprising 3 owned sites and 37 leased sites of which 3 are sublet. This portfolio gives rise to risks in relation to ongoing lease costs, dilapidations and fluctuations in value.

#### Working capital

The Group has a significant investment in working capital in the form of trade receivables and inventories. There is a risk that this investment is not fully recovered.

#### Financial liquidity, debt covenants and interest rates

The Group needs continuous access to funding to meet its trading obligations and to support organic growth and acquisitions. There is a risk that the Group may be unable to obtain funds or that such funds will only be available on unfavourable terms. The Group's borrowing facility comprises a committed facility of up to £30 million. This includes requirements to comply with specified covenants, with a breach potentially resulting in Group borrowings being subject to more onerous conditions.

#### Decentralised structure

The Packaging Distribution business model reflects a decentralised approach with a dependency on effective local decision-making. There is a risk that the decentralised management control is less effective and local decisions do not meet corporate objectives.

#### Defined benefit pension scheme

The Group's defined benefit pension scheme is sensitive to a number of key factors; investment returns and the discount rates as well as mortality assumptions used to calculate scheme liabilities. The IAS 19 valuation of the Group's defined benefit pension scheme as at 31 December 2019 estimated the scheme deficit to be £6.5 million, a decrease of £3.3 million during 2019. Small changes in these assumptions could mean that the deficit increases.

#### Acquisitions

The Group's growth strategy includes acquisitions as demonstrated in recent years. There is a risk that such acquisitions may not be available on acceptable terms in the future. It is also possible that acquisitions will not succeed due to the loss of key people or customers following acquisition or the acquired business not performing at the level expected. This could potentially lead to an impairment in the carrying value of the related goodwill and other intangible assets. Execution risks around the failure to successfully integrate the acquired business after the conclusion of the earn-out period also exist.



Mitigating factors	Change in 2019
<ul style="list-style-type: none"> <li>The Group works closely with suppliers to manage the scale and timing of price supplier price movements to end-users effectively.</li> <li>Our IT systems monitor and measure effectiveness in these changes.</li> <li>Where possible, alternative supplier relationships are maintained to minimise supplier dependency.</li> <li>We work with customers to redesign packs and reduce packing cost to mitigate the impact of cost increases.</li> </ul>	 no change
<ul style="list-style-type: none"> <li>Where a site is non-operational the Group seeks to assign, sell or sub-lease the building to mitigate the financial impact.</li> <li>If this is not possible, rental voids are provided on vacant properties taking into consideration the likely period of vacancy and incentives to re-let.</li> </ul>	 no change
<ul style="list-style-type: none"> <li>Credit risk is controlled by applying rigour to the management of trade receivables by our Credit Manager and the credit control team, and is subject to additional scrutiny from the Group Finance Director.</li> <li>Inventory levels and order patterns are regularly reviewed and risks arising from holding bespoke stocks are managed by obtaining order cover from customers.</li> </ul>	 no change
<ul style="list-style-type: none"> <li>The Group seeks to maintain an appropriate level of committed bank facilities that provide sufficient headroom above peak projected borrowing requirements.</li> <li>The existing facility is in place until June 2022.</li> <li>The Group regularly monitors net bank debt and forecast cash flows to ensure that it will be able to meet its financial obligations as they fall due.</li> <li>Compliance with covenants is monitored on a monthly basis and sensitivity analysis is applied to forecasts to assess the impact on covenant compliance.</li> </ul>	 no change
<ul style="list-style-type: none"> <li>The Group ensures that our staff have the right working environment, information and sales tools to enable them to meet corporate objectives.</li> <li>A comprehensive management information system is maintained with key performance indicators monitored and actions taken when required.</li> </ul>	 no change
<ul style="list-style-type: none"> <li>The scheme was closed to new members in 2002.</li> <li>Benefits for active members were amended by freezing pensionable salaries at 30 April 2009 levels.</li> <li>A Pension Increase Exchange option is available to offer flexibility to new pensioners in the current level of pension benefits and the rate of future increases.</li> <li>The Group makes Deficit Reduction Contributions each year.</li> <li>The investment profile is regularly reviewed to ensure continued matching of investments with the liability profile of the scheme with details set out in note 25.</li> </ul>	 decreased
<ul style="list-style-type: none"> <li>The Group carefully reviews potential acquisition targets, ensuring that the focus is on high-quality businesses which complement the existing Group profile and provide opportunities for growth.</li> <li>Having completed a number of acquisitions in recent years, the Group has well-established due diligence and integration processes and procedures.</li> <li>The Group has a comprehensive management information system to enable effective monitoring of post-acquisition performance.</li> <li>Earn-out mechanisms also mitigate risk in the post-acquisition period.</li> <li>Goodwill and other intangible assets are tested annually for impairment with the results set out in note 10.</li> </ul>	 no change

## Stakeholder engagement

The Board and its individual Directors consider that they have acted in good faith in the manner that is most likely to promote the success of Macfarlane Group for the benefit of its members as a whole and in doing so having regard to the stakeholders and matters set out in Section 172 of the Companies Act 2006.

There is a recognition by the Directors that they are not expected to balance the interests of Macfarlane Group against those of other stakeholders but rather, after considering all relevant factors, to decide on the actions which will best lead to success for the Group having regard to the long term. This can mean that certain stakeholder groups may be inadvertently adversely affected, but this will not of itself call into question the decisions made.

The Directors view the key Company stakeholders and means of engagement as shown in the table below.

In all cases, the level of engagement informs the Board, both in relation to stakeholder concerns and the likely impact on decision-making throughout the year.

We expect our people to act with the highest level of integrity in dealing with all stakeholders. We operate a suite of policies which are intended to ensure that Macfarlane employees are empowered to make decisions locally but within a control framework which meets the Group's objectives.

The Board uses its regular meetings as a mechanism to address and meet its obligations under Section 172 of the Companies Act 2006. The following narrative on pages 20 and 21 covers the key decisions made and the stakeholder group(s) impacted by these decisions.

### Strategy and performance

#### Strategy 1 2 3 4 5

The Board reviews the Group's strategic direction and growth plans during each calendar year.

The Board approved the two acquisitions in the Packaging Distribution business, concluding that both businesses had a similar customer and business approach to Macfarlane and would be a good strategic fit.

Each year the Board reviews and approves Corporate Defence documents designed to protect the value of Macfarlane Group in the event of an unexpected approach.

#### Performance 1 2 3 4

The Board approves the annual budget for the forthcoming year at its December meeting.

The Board reviews the trading performance of the business throughout the year, monitoring performance against the agreed budget and the previous financial year.

At each meeting the Board receives reports from the Chief Executive and the Finance Director. These reports cover trading performance, relationships with key customers and suppliers as well as aspects of operational performance and the impact on our employees. The reports also give the Board visibility of the up to date trading terms with both customers and suppliers.

During 2019, the Board met with representatives of one of our strategic supply partners for paper-based products.

The activities of our competitors are reviewed, along with any potential impact on the Group.

Stakeholder Group	Principal methods of engagement
1 Shareholders	Members of the Board engage with shareholders throughout the year at events such as the Annual General Meeting, the results roadshows and Capital Markets Days. Our Chairman also meets with major shareholders each year. This gives shareholders a number of opportunities to raise concerns.
2 Employees	The Board holds at least four of its meetings at different Group locations and this provides the opportunity to engage with the local teams and hear their views on working in Macfarlane Group.
3 Customers	Teams at all our locations interact with all our existing and potential customers, in the Local, Core and National customer groups on a daily basis to understand and fulfil the product and service requirements of our customers.
4 Suppliers	Our procurement teams and employees at all our locations interact both with our strategic and all other suppliers on a daily basis to ensure that the supply chain is robust and that the trading relationships with suppliers continue to operate well.
5 Our trading locations and the impact of our activities on the local environment	We operate from good quality facilities throughout the UK and deliver to customers using our own fleet of trucks, driven by our drivers. We act in a manner intended to recognise and reduce our impact on our local environments in terms of the types of product supplied, usage of energy and CO <sub>2</sub> emissions.

## Financing 1 2 5

The Board approves the terms and conditions attaching to the Group's major banking arrangement and receives a monthly report confirming compliance with bank covenants.

The Board approves the annual dividend, taking into account distributable reserves and likely cash flows and the level of dividends relative to other financing requirements.

At the conclusion of each triennial actuarial valuation of the pension scheme deficit, the Board approves the contributions being proposed under the recovery plan for any deficit.

The Board approves all location moves and the terms of new property arrangements. This included the closure of our Enfield site in September 2019 and the move to a smaller site in Harlow, supported by additional space in Sudbury as well as the closure of a small manufacturing site in Nether Broughton and the transfer of that trade to an existing site in Nottingham.

The Board considers and approves any items of capital expenditure with a value in excess of £100k. During 2019 the major item of capital expenditure was for a new printing press in our Labels business in Ireland at a cost of c. £800k.

Major capital allocation decisions are a matter reserved for the Board.

## Risk 1 2 3 4 5

The Board reviews the Company's internal control framework ensuring regular updating of the business's risk registers.

The Board regularly reviews the Group's risk register, ensuring that where appropriate and practical, there are monitoring procedures, mitigating controls and actions in respect of each major risk. This includes a formal consideration of emerging risks.

The Board receives a Health and Safety status report at every meeting as well as an annual presentation from the Group's Health & Safety Manager, which covers the impact on our employees, our sites and our local environment.

The Audit Committee confirms to the Board that the Internal Audit Plan has been completed and that all internal audit reports have been considered and action taken where necessary.

## Governance and legal requirements 1 2

The Board conducts an annual review of its effectiveness and the effectiveness of the Board Committees.

The Board considers the current and future composition of the Board, with a focus on diversity and Board capabilities and reviews succession planning for both Executive and Non-executive Directors to ensure orderly succession.

The Board reviews the Annual Report, confirming that in its view the Annual Report is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

The Board reviews and satisfies itself with all other trading updates, including the AGM statement, the half-year report and a trading update in the final quarter of the year.

The Board accepted the Audit Committee's recommendation to appoint Deloitte LLP as external auditor.

## Culture and organisation 1 2

The Board seeks to satisfy itself that the Group's policies and practices for staff are consistent with the Company's values and are designed to promote the long-term success of the Group.

Andrea Dunstan was appointed as our nominated Employee Director given her recent and relevant experience in this area.

The Remuneration Committee reviews the remuneration packages for the Executive Directors and the Chief Executive's key reports each year.

The Board reviews annual pay increases for Executive Directors each year, ensuring these are consistent with the wider employee group, ensuring that these are appropriate and consistent.

The Board reviews and approves the Group's Gender Pay reports each year.

The Board receives a report from the HR Director each year covering key employee matters and developments. This report covers the results of our annual employee survey.

Representatives of the Board engage with the Management Development Group and attend the Annual Awards Dinner.



## Viability statement

### **The Board has considered the Group's viability as part of the ongoing programme to manage risk.**

Each year the Board reviews the Group's strategic plan for the forthcoming three-year period and challenges the Executive team on the plan's risks. The strategic plan reflects the Group's businesses, which have a broad spread of customers across a range of different sectors with some longer term contracts in place. The assessment period of three years is consistent with the Board's review of the Group strategy, including assumptions regarding future growth rates for our business and acceptable levels of performance.

A detailed financial model covering the three year period is maintained and regularly updated. The model is subject to sensitivity analysis which includes flexing a number of the main assumptions, including future revenue growth, gross margins, operating costs, finance costs and working capital management. The results of flexing these assumptions, both individually and in aggregate, are used to determine whether additional bank facilities will be required during the three-year period. The results of the exercise indicated that no additional facilities should be required.

The Board has carried out a thorough assessment of the principal risks facing the Group and how these risks affect the Group's prospects and the strategic plan. The review also includes consideration of the principal risks facing the Group as described on pages 18 and 19, which could prevent the Group from achieving its strategic plan and the potential impact these risks could have on the Group's business model, future performance, solvency and liquidity over the next three years.

The Directors' assessment has been made with reference to the resilience of the Group and the strength of its financial position, the Group's current strategy, the Board's risk appetite and the Group's principal risks including how these are managed. The Board is confident that the Group's major banking facility, which runs until 30 June 2022, would be renewed on terms similar to those currently in place.



## Corporate responsibility

Macfarlane Group has a responsibility to ensure that through its business operations it impacts positively on society. To achieve this, we have a series of three programmes focused on environmental care, improving the customer experience and increasing employee engagement.

Corporate Responsibility ('CR') leadership comes from an internal committee consisting of members from a cross section of the Group led by the Director of Group Risk. The key objectives of the CR Committee are:

- To improve the awareness of CR across the Group;
- To develop and implement action plans that support the CR strategy;
- To ensure that CR is an integral part of daily operational activities; and
- To monitor and report on CR performance using agreed key performance indicators.

### Environmental care

#### Mandatory Greenhouse Gas Reporting 2019

Macfarlane Group seeks to minimise the impact of our operations on the environment and is committed to reducing its greenhouse gas ('GHG') emissions. This report outlines Macfarlane's GHG emissions for 2019. Using an operational approach, the Group identified its boundaries to ensure all activities and facilities for which it is responsible were being recorded and reported in line with Scope 1 and 2 of the Mandatory Greenhouse Gas Reporting regulation. Relevant data was provided to an independent consultant, EcoAct. The validity, accuracy and completeness of the data was audited by EcoAct and then used to calculate the GHG for Macfarlane Group. Calculations were completed in accordance with the main requirements of ISO-14064-1:2006 standard and deliver both absolute values and an intensity ratio for Macfarlane's emissions. Acquisitions made during 2019 have been included in GHG reporting and an assumption has been made regarding usage based on equivalent Group sites.

Macfarlane Group uses total turnover (£000) in the reporting period to calculate the intensity ratio, as this allows emissions to be monitored over time taking into account changes in the size of the Group. This factor was chosen because it provides the greatest degree of accuracy and is the metric best aligned to business growth.

The results in tables 1 and 2 show that total gross GHG emissions in the period were 6,752 tonnes of CO<sub>2</sub>e, (2018: 7,297 tonnes) comprised of the following:

- **Direct Emissions (Scope 1)**  
**5,312 tonnes of CO<sub>2</sub>e – 79%**  
(2018: 5,646 tonnes – 77%)
- **Indirect Emissions (Scope 2)**  
**1,440 tonnes of CO<sub>2</sub>e – 21%**  
(2018: 1,651 tonnes – 23%)

72% of emissions came from diesel, 21% from electricity, and 7% from natural gas.

Broken down by business unit the results were as follows:

- **Packaging Distribution**  
**5,412 tonnes of CO<sub>2</sub>e – 80%**  
(2018: 5,277 tonnes – 72%)
- **Manufacturing Operations**  
**1,340 tonnes of CO<sub>2</sub>e – 20%**  
(2018: 2,020 tonnes – 28%)

**Table 1: Type of emissions**

Type of emissions	Activity	2019 Units	2018 Units	2019 Tonnes of CO <sub>2</sub> e	2018 Tonnes of CO <sub>2</sub> e
Direct (Scope 1)	Natural gas (kWh)	2,435,349	2,940,503	448	541
	Vehicle fuel (litres)	1,822,058	1,932,382	4,718	5,078
	Other	23,512	825	146	27
	Subtotal			5,312	5,646
Indirect (Scope 2)	Purchased electricity (kWh)	5,360,779	5,828,517	1,440	1,651
	Subtotal			1,440	1,651
Total gross emissions (tCO <sub>2</sub> e)				6,752	7,297

**Table 2: Intensity ratio**

	2019	2018
Total gross GHG emissions (tCO <sub>2</sub> e)	6,752	7,297
Total sales (£000)	225,389	217,290
Carbon intensity (tCO <sub>2</sub> e/£000)	0.030	0.034

## Corporate responsibility (continued)

As set out in Table 3 below, Manufacturing Operations have a proportionately higher impact on emissions than the Distribution business. However recent investments in Labels are focusing on moving from high carbon intensity activities to lower carbon methods such as digital printing.

Macfarlane's overall footprint decreased 7.5% from 7,297 tonnes to 6,752 tonnes. The intensity calculation for 2019 reflects the work completed with a reduction in emissions based on turnover from 0.034 to 0.030.

This is predominantly due to a switch to hybrid petrol vehicles with reduced consumption at some manufacturing sites. However, decreasing electricity emission factors caused by decarbonisation of the national grids of the UK and Ireland has also been significant.

Emissions from natural gas consumption decreased by 17% at least partly due to a warm 2018/19 winter.

Electricity consumption decreased by 7.3% which, due to the decarbonisation of the UK and Ireland national grids, resulted in emission reductions from purchased electricity of 11.8%.

Emissions from diesel fuel decreased by 11.3%, largely driven by a shift to diesel reclaims, but also to a lesser extent by a slight material increase in usage of petrol hybrid vehicles.

Our policy of leasing the vast majority of our premises allows us to vary our property footprint to ensure the maximum efficiency of our operations, thereby minimising the impact on the environment.

Given the growth of the business, continued reductions in the overall Gross tCO<sub>2</sub>e/Sales result will be a challenging target, however the Group is committed to see a further year on year reduction in 2020.

### Taskforce on Climate-related Financial Disclosures (TCFD)

Macfarlane Group supports the recommendations of the Financial Stability Board's TCFD and continues to make progress in our consideration and response to the issue of climate change.

The Board considers climate change risk as part of its risk management oversight. Areas where climate related risks could impact the business include increased raw material prices, increased business interruption and/or reduced economic activity due to the increased frequency of extreme weather incidents.

Climate related risks and opportunities are an integral part of the Macfarlane Group strategy as we seek to provide our customers with the information and options to allow them to make better informed decisions about the impact of our products and services on the environment. Packaging is an essential commodity for many businesses, but it is important to consider ways to minimise the impact that packaging can have on the environment, without compromising on product protection.



### Environmental impact rating



Packaging and labels are essential commodities for many businesses, but it is important to consider ways to minimise the impact that both can have on the environment, without compromising on product protection.

**Table 3: Business segment**

Business segment	2019 Tonnes of CO <sub>2</sub> e	2018 Tonnes of CO <sub>2</sub> e	2019 Sales £000	2018 Sales £000	2019 tCO <sub>2</sub> e/£000	2018 tCO <sub>2</sub> e/£000
Packaging Distribution	5,412	5,277	196,706	189,835	0.028	0.028
Manufacturing Operations	1,340	2,020	28,683	27,455	0.047	0.074
Total	6,752	7,297	225,389	217,290	0.030	0.034



Further information can be found on our website at [www.macfarlanegroup.com/corporate-responsibility/environment](http://www.macfarlanegroup.com/corporate-responsibility/environment).

The assessment of climate related risks and opportunities is an ongoing area of focus for Macfarlane Group and further work is planned to fully understand the impact of climate change on our business and to ensure that we have the appropriate mitigation in place to mitigate these risks.

### Waste management

The Group's overall waste tonnages decreased despite additional sales and further acquisitions, maintaining our waste management objectives to deliver a high recycling and recovery rate. This has been achieved during 2019 with support from Reconomy initially and then by Footprint Recycling, our new waste management service provider, during the year. We have been able to carry out more site audits at our facilities, local toolbox talks, and providing reports to help manage waste streams and costs together with implementing continuous improvement programmes in monitoring waste volumes and increasing segregations of waste streams. Not all of our sites were supported by Reconomy and Footprint Recycling in 2019 and therefore assumptions have been made in the collection of certain data.

Our goal to achieve a 'zero to landfill' status in 2019 was very close with all businesses across the Group achieving over 98.3% of waste diverted from landfill. The levels of waste segregated on site increased to 73% (2018: 67%).

Our Labels division, through recycling 50 tonnes (2018: 69 tonnes) of paper-based backing product as part of their waste reduction programme, again achieved the best result in the Group with 99.9% (2018: 99.9%) waste diverted from landfill.

Table 4 demonstrates significant improvements in the recycling and recovery rate figures in the last ten years.

Further achievements in 2019 are:

- The majority of Macfarlane sites now purchase electricity through renewable sources.
- Four of our sites are now registered as FSC® accredited, facilitating the procurement and distribution of sustainably sourced products.

Our key environmental objectives for 2020 include:

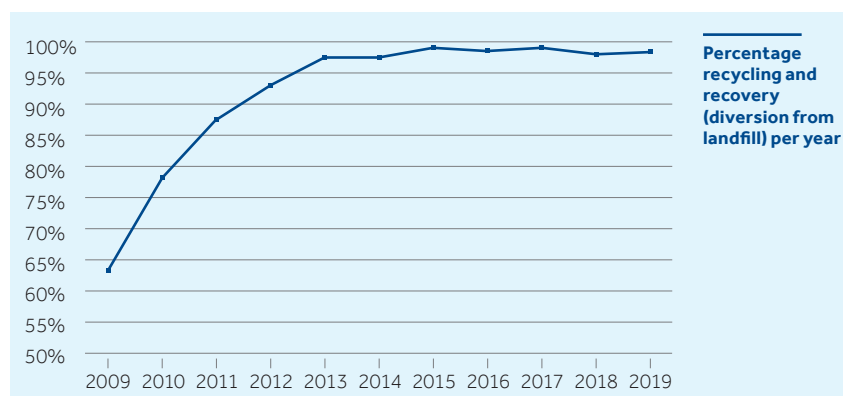
- Continuous review and appraisals of all sites every quarter with a view to making efficiencies;
- Consider options for capital expenditure to improve efficiency in the Group's recovery and recycling activities, taking into account the findings from our Energy Savings Opportunity Scheme ('ESOS') report;

- Incorporate all new sites under the Group waste contract therefore ensuring compliance, regular reviews and appraisals to support the overall Group targets;
- Continuation of our programme to introduce LED lighting throughout our sites;
- Deliver savings through the Manufacturing Waste Reduction Programme;
- Develop a transition plan to register recent acquisitions to BSI ISO 14001 Environmental Management Standard; and
- Increasing the number of sites capable of selling products which are FSC certified as coming from sustainable sources.

Macfarlane Group works in partnership with its customers and suppliers to ensure that we provide an expert, independent and tailored approach, which takes into consideration the impact which the products and services we provide have on the environment.

One approach we take to achieve this is by using an Environmental Product Matrix, produced in conjunction with our suppliers, which is consistent with the underlying need to ensure products are effectively protected in storage and transit. This Matrix enables our customers to choose packaging, which is fit for purpose, whilst ensuring they still embrace the Reduce, Re-use, and Recycle ethos.

**Table 4: Recycling and recovery rate**



## Corporate responsibility (continued)

To support our ongoing commitment to improve our environmental performance, we pursue the following objectives:

- To ensure compliance with all applicable environmental legislation and regulations;
- To reduce emissions' pollution;
- To improve waste management practices;
- To reduce the consumption of natural resources;
- To minimise noise and other nuisances; and
- To continuously assess our environmental performance.

These objectives are monitored by an internal independent audit process providing visibility of a site's operational activities and its adherence to legislative or Company requirements. Environmental information is recorded, reviewed and analysed, by an identified team to ensure compliance with the Company's legal obligations and achievement of internal objectives and targets.

The Group continues to make progress in its performance against the identified CR objectives. During 2020, the CR Committee will continue to review environmental performance, actively supporting methods or practices that contribute to the continued development of a culture driven by environmental responsibility.

### Registration to ISO 14001

With the exception of certain recent acquisitions, all our UK packaging sites are registered to BSI ISO 14001 Environmental Management Standard. As an internationally recognised standard on environmental management, registration involves a process of continual assessment of our environmental standards and processes. A key objective in 2020 is the development of a transition plan to register recent acquisitions under the standard.

### Health and Safety

The health, safety and welfare of all people, including colleagues, customers and suppliers, forms a critical part of Macfarlane Group's business objectives. We aim to achieve a positive health and safety culture through the creation of a safe and healthy work environment, preventing and minimising risks. Our vision and goals for Health and Safety and how we commit to achieve them are based upon the best practice guidelines, issued by the Health and Safety Executive. To ensure we adhere and abide by best health and safety practices we have dedicated Health and Safety Managers in the business, who work with local Health and Safety teams to ensure knowledge and standards are effectively applied to the business on a consistent basis throughout all the health and safety disciplines.

We continue to invest in our premises and our equipment to improve the safety of our business operations, particularly in relation to the operation of our machinery and vehicles.

The Accident Frequency Rate ('AFR') representing the number of reportable incidents per 100,000 man-hours worked is shown in Table 5.

In 2019, we experienced a decrease in AFR vs. 2018. This represented 4 reportable incidents compared to 11 in 2018. All reportable incidents are investigated thoroughly by our Health & Safety team and changes to working practices implemented if required. We also ensure that training in a particular area where incidents have arisen is reinforced. Manual handling and slips, trips and falls are the highest causes of reportable incidents and we continue to review and improve our training and oversight of these activities as part of our ongoing commitment to the safety of our people.

In 2019, the business focused on behavioural health and safety, including incident reporting, safety observations and providing feedback on safety performance.

Key achievements in 2019 included the following:

- Reduction in accident frequency rate to lowest figure for 4 years;
- Launch of new Safe Operating Procedures across Packaging Design and Manufacture Operations and Group Logistics, as part of a rolling programme of review and development;
- 178% increase in reporting of Safety Observations including Positive Safety Observations, which were introduced in 2019 to encourage sharing of good practice across the Group;
- Introduction of award scheme to encourage the reporting of safety observations; and
- New online safety awareness training introduced.

**Table 5: Accident Frequency Rate (AFR)**

Business segment	2019	2018	2017	2016	2015
Packaging Distribution	<b>0.15</b>	0.48	0.53	0.42	0.34
Manufacturing Operations	<b>0.43</b>	1.20	0.22	1.11	0.46
<b>Group</b>	<b>0.23</b>	0.73	0.43	0.64	0.38

In 2020, our aim is to maintain our continuous improvement approach to health and safety at Macfarlane Group through:

- Encouraging and promoting good working practices;
- Ongoing development of Safe Operating Procedures;
- Increased identification and reporting of leading indicators;
- Root cause analysis of all incidents, accidents and high potential near misses; and
- Continued increase in the number of Senior Management Safety Checks being conducted.

We also recognise our commitment to the safety of our drivers and those who share the roads with our delivery vehicles. We now have camera systems fitted to many of our vehicles and the roll out of this initiative continues as part of our commitment to continuous improvement in our health and safety performance.

To ensure constant and consistent focus regarding Health and Safety throughout the Group, it is a main agenda item at all formal monthly review meetings and operating sites in the Group are internally assessed and graded on their Health and Safety performance.

The Group Board plays a key role in overseeing the operation of all Health and Safety, reviewing reports on Health and Safety at each meeting. This report covers incidents, near misses, reportable and non-reportable incidents.

## Customer experience

### Customer feedback

To continually improve the service to our customers, we use a range of metrics to evaluate our performance on an annual basis. In Packaging Distribution, we gain regular feedback from our customers through Net Promoter Score (NPS) Surveys, an Annual Customer Satisfaction Survey, Mystery Shopper and online Trust Pilot reviews. This feedback is then used to improve products, processes and systems that interact with our customers. In addition, we continue to survey our customers in all of our businesses, on an annual basis, to evaluate our performance against a range of key service metrics.

### Sales order management

Our online customer order management and e-trading system, Simplicit.e, and [www.macfarlanepackaging.com](http://www.macfarlanepackaging.com) are contributing to improvements in productivity as well as meeting the needs of our customers requiring more visibility of their packaging management. In the Packaging Distribution business in 2019, the percentage of sales transacted online has decreased from 11.5% to 9.5% and order lines transacted online increased to 23% vs. 22% in 2018.

### Electronic documentation

In 2019, 91% (2018: 88%) of invoices to our customers were delivered electronically, further reducing our paper usage. The Group is continuing to encourage customers to receive documentation electronically.

**Table 6: Annual customer satisfaction scores**

	2019	2018
Packaging Distribution	<b>93%</b>	90%
Packaging Design and Manufacture	<b>85%</b>	89%
Labels	<b>91%</b>	96%



## Corporate responsibility (continued)

### Employees

Macfarlane Group understands the importance of connecting with, engaging and rewarding its people as well as recognising the importance of meaningful communication and consultation in maintaining good employee relations. The ability to attract and retain the very best people is crucial to ensuring the growth of the business. As such, maintaining a working environment that promotes employee well-being, personal development and positive employee relations, at every level is paramount.

#### Employee development

The Group encourages an environment which gives individuals the opportunity to develop their careers and reach their full potential. Through a variety of learning opportunities and initiatives that are designed to help employees develop their skills the Company provide a platform for personal development creating opportunities for individual growth whilst ensuring employees have the correct skills and knowledge to provide an outstanding service to our customers.

The continued engagement with apprenticeship schemes, alongside the investment in both internal and external training programmes, including the Macfarlane Leadership Programme, aimed at supporting the development of future leaders, has seen an increase in training hours for the Packaging and Labels business in 2019 to 16 hours per employee. The Group, including acquisitions has provided on average 15 hours of training per employee during 2019.

In addition to traditional methods of training, the provision and encouragement of on-line training programmes has supported all employees to engage in their personal development, irrelevant of role or geographical location.

The Company also provides Sponsored Further Education programmes, to support employee engagement in long-term education.

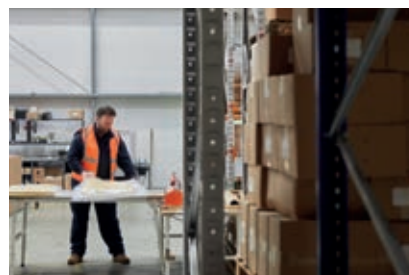
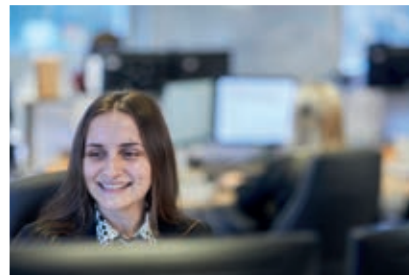
#### Employee engagement

Macfarlane Group use a number of ways to engage and communicate with employees on a regular basis. Through business update sessions, functional forums and informal review meetings a platform is provided for employee participation and involvement. A number of tools are also used in order to obtain employee feedback including targeted employee questionnaires and workshops. These forums along with annual appraisals, departmental meetings and individual one-to-one discussions provide an opportunity for our employees, to engage in an open two-way dialogue covering topics including business performance, strategic targets and the overall wellbeing of our employees.

Interactive tools are also provided to employees via mechanisms such as tablets enabling employees to gain information, advice and provide feedback instantly. In addition to supporting engagement with the employee these interactive tools support the provision of outstanding customer service.

Company policy is to encourage the employment of disabled persons where the disabilities do not hinder these persons in the performance of their duties. Where an employee becomes disabled every effort is made to re-settle that employee in a suitable post. Registered disabled persons, once employed, receive equal opportunities for training, career development and promotion.

Engagement in local communities and supporting charities is encouraged. During 2019, we supported events either from a resource or a financial perspective. Each year Macfarlane Group makes a one-off donation to a charity chosen by the workforce; for 2019 this was Cancer Research UK.



Macfarlane Group provides a platform for personal development whilst ensuring employees have the correct skills and knowledge to provide an outstanding service to customers.

## Diversity

The gender breakdown of Directors, Senior Managers and other Group employees at the year-end is shown in Table 7.

### Gender Pay Gap

Macfarlane Group reported its Gender Pay Gap information in April 2019. This showed men's mean hourly rate to be 12.9% higher than women's and women's median hourly rate to be 9.9% higher than men's. The median pay gap in favour of women is reflective of the fact that our sales function is predominantly female, while the lower earning band of employees in production and logistics is predominantly male. These results do however change when reviewing the mean pay gap information. This is reflective of the demographics of the Senior Executive team and those printers (typically male) employed within Macfarlane Labels as skilled professionals, who receive competitive basic pay and a full shift system, offering a significant uplift on standard hourly rates.

Further details can be found on our website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)).

### Human Rights

Macfarlane Group does not have a specific Human Rights policy at present but it does have other policies, which reflect established human rights' principles. These are:

- Equality – Macfarlane Group is committed to providing equal opportunities in employment and to avoiding unlawful discrimination in recruitment, employment or to its customers and suppliers. Striving to ensure that the work environment is free of harassment and bullying and that everyone is

treated with dignity and respect is an important aspect of ensuring equal opportunities in employment and there is a specific dignity at work policy, which deals with these issues. Where an employee becomes disabled every effort is made to ensure that their employment with the Group continues and that appropriate adjustments are made. Disabled employees receive equal opportunities regarding selection for training, career development and promotion.

- Engagement – Macfarlane Group recognises the importance of meaningful communication and consultation in maintaining good employee relations. This is achieved through formal and informal meetings across all business units.
- Anti-Bribery & Corruption – Macfarlane Group has an anti-bribery and corruption policy, which is supplemented by a gift register and an associated policy on accepting gifts.
- Whistleblowing policy – there is provision for employees to use an independent service if they are not comfortable speaking to anyone within Macfarlane Group with regard to any matters which give them concern. This service is promoted throughout the Group.
- Modern Slavery Act – Macfarlane Group has now made a statement under the Modern Slavery Act which is supported by internal procedures to ensure that the principles of the act are adhered to. The statement is available on the website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)).

No material breaches of the above policies were noted during 2019, nor were any matters of significant concern reported through our whistleblowing service.

## Non-financial reporting regulations

In considering the requirement of Non-financial reporting regulations, we have summarised below where further information on each of the key areas of disclosure is provided.

- The description of business model is set out on pages 6 and 7.
- Main trends/factors likely to affect the future development, performance and position of the business are set out in the Business and Financial reviews in the Strategic Report on pages 4 to 29.
- Description of principal risks and adverse impacts are set out in the Strategic Report on pages 18 and 19.
- Non-financial KPIs are included throughout the report in both the business model section and the corporate responsibility report.
- Commentary on Environmental matters, Employees, Social and Community matters, Human Rights and Anti-Bribery and Corruption are included in the Corporate Responsibility Report on pages 23 to 29.

**Table 7: Diversity**

	2019		2018	
	Female	Male	Female	Male
Directors	1	5	1	5
Senior Managers	5	12	5	12
All other employees	320	575	306	560

## Board of Directors



1



2



3



4



5



6

### 1 Stuart Paterson Chairman

Stuart joined the Board on 1 January 2013 as a Non-executive Director, becoming Chairman on 29 September 2017. He is a Chartered Accountant and was Chief Financial Officer at Forth Ports Limited until he retired in January 2018. He joined Forth Ports in March 2011 when it was listed on the London Stock Exchange and the company was subsequently acquired by Arcus Infrastructure Partners in 2011. Prior to this role, Stuart was Chief Financial Officer of Johnston Press PLC from 2001 to 2010 and previously worked in senior financial management roles at Motorola Corporation, and as Group Finance Director and then Managing Director Europe for Aggreko PLC. Stuart joined Angel Trains Group Limited as a non-executive Director in September 2018, and chairs the Audit & Risk Committee. He is also a trustee of the Royal Yacht Britannia and a member of their Audit, Risk and Remuneration Committees. He also served as a non-executive Director with Devro PLC from 2006 to 2012, chairing the Audit Committee. He chairs the Nominations Committee and is a member of the Remuneration Committee.

### 2 Peter Atkinson Chief Executive

Peter joined Macfarlane Group as Chief Executive in October 2003. He has a strong sales and marketing background through his career at Procter & Gamble and S.C. Johnson. Peter also has significant general management experience gained during his time at GKN PLC and its joint venture partners where he worked from 1988 to 2001 in a number of senior executive roles in their business-to-business operations. He has a successful track record of both business turnarounds and business development with extensive exposure to international business, having worked in the UK, Europe and the USA.

### 3 John Love Finance Director

John is a member of The Institute of Chartered Accountants of Scotland and has been with the Group for twenty-four years and was appointed Finance Director on 12 July 1999. He was with Deloitte and its predecessor firms for sixteen years before joining Macfarlane Group in 1996.

### 4 Bob McLellan Non-executive Director and Senior Independent Director

Bob joined the Board on 5 March 2013. He was Chief Executive of DS Smith Packaging UK until 2011, latterly as Deputy CEO Packaging (UK and Continental Europe). Bob has spent many years working in the packaging sector and has held leading roles in both the UK and Continental Europe for industry employer associations. He is currently Chairman of the Logson Group and a non-executive director of Swanline Print Limited. Bob chaired the Remuneration Committee until 31 August 2018 when he was appointed as the Group's Senior Independent Director. He is a member of the Nominations, Remuneration and Audit Committees.





#### 5 **James Baird** Non-executive Director

James joined the Board on 8 January 2018. James previously led the Scotland and Northern Ireland business of Deloitte, the global accountancy firm, before becoming Managing Partner of its Audit & Risk Advisory division and Chief Operating Officer, both in Switzerland. An experienced auditor and advisor who has worked with companies in the UK and Europe across a range of industries, he is currently an Honorary Professor at Glasgow University's Adam Smith Business School. James is a member of both the Research Panel and the Technology Advisory Group of the Institute of Chartered Accountants of Scotland. James was appointed as chair of the Audit Committee on his appointment on 8 January 2018 and is a member of the Remuneration and Nominations Committees.

#### **Derek Quirk** Company Secretary

Derek joined Macfarlane Group in December 2015 as Director of Group Risk. He was appointed Company Secretary on 1 March 2016 and is a member of the Group's Executive Committee. He provides legal support and leads the Group's Internal Audit function. Prior to his current role, Derek was with BBA Aviation PLC for seven years, serving as Head of Group Internal Audit and latterly as Financial Controller for one of the company's divisions. He is a member of The Institute of Chartered Accountants of Scotland.

#### 6 **Andrea Dunstan** Non-executive Director

Andrea joined the Board on 1 September 2018 and has significant experience in the areas of performance management, organisational development, strategy and change management across several sectors notably distribution and third party logistics. She was most recently Chief People Officer at Premier Farnell PLC. Andrea is a non-executive Director of Sumo Group PLC, where she is chair of the Remuneration Committee and a member of the Audit and Nominations Committees. She is also a Non-executive Director and Chair of the Remuneration Committee at TI Fluid Systems PLC. Andrea is a member of the Executive Council of The University of Salford where she also chairs the Remuneration Committee. Andrea was appointed as chair of the Remuneration Committee on her appointment on 1 September 2018 and is a member of the Audit and Nominations Committees.

## Corporate information

**Registration number**  
No. SC 004221  
Registered in Scotland

**Company Secretary**  
Derek L.H. Quirk

**Registered office**  
3 Park Gardens  
Glasgow G3 7YE  
Telephone: 0141 333 9666  
Email: [info@macfarlanegroup.com](mailto:info@macfarlanegroup.com)

**Principal bankers**  
Lloyds Banking Group PLC  
110 St. Vincent Street  
Glasgow G2 5ER

**Solicitors**  
CMS Cameron McKenna  
Nabarro Olswang LLP  
Saltire Court  
20 Castle Terrace  
Edinburgh EH1 2EG

Wright Johnston & Mackenzie LLP  
302 St. Vincent Street  
Glasgow G2 5RZ

**Stockbrokers**  
Arden Partners plc  
125 Old Broad Street  
London EC2N 1AR

**Independent auditor**  
Deloitte LLP  
110 Queen Street  
Glasgow G1 3BX

**Registrars**  
Equiniti  
Aspect House  
Spencer Road  
Lancing  
West Sussex BN99 6DA

## Report of the Directors

**The Directors present their annual report and the audited financial statements of the Group for the year ended 31 December 2019. Pages 4 to 51 inclusive comprise the Directors' report, which in turn includes the Strategic Report on pages 4 to 29.**

These reports have been drawn up and presented in accordance with and in reliance upon applicable company law and any liability of the Directors in connection with these reports shall be subject to the limitations and restrictions provided by such laws.

### Corporate governance

The information that fulfils the requirement of the Corporate Governance Statement can be found in the Corporate Governance Section on pages 44 to 51 (and is incorporated into this report by reference) with the exception of the information referred to in the Financial Conduct Authority Disclosure and Transparency Rules 7.2.6, which is located within this report.

### Report on greenhouse gas emissions

Details of the Group's emissions and policies are contained within the Corporate Responsibility Report.

### Cautionary statement

The Chairman's Statement and the Strategic Report have been prepared to provide additional information to members of the Company to assess the Group's strategy and the potential for the strategy to succeed. It should not be relied on by any other party or for any other purpose.

This report and the financial statements contain certain forward-looking statements relating to operations, performance and financial status. By their nature, such statements involve risk and uncertainty because they relate to events and depend upon circumstances that will occur in the future. There are a number of factors, including both economic

and business risk factors, which could cause actual results or developments to differ materially from those expressed or implied by these forward-looking statements.

These statements are made by the Directors in good faith based on the information available to them up to the time of their approval of this report. Nothing in this report and the financial statements should be considered or construed as a profit forecast for the Group.

### Results and dividends

The Group's profit before tax from continuing activities was £12,024,000 (2018: £10,886,000). This resulted in a profit for the year of £9,731,000 (2018: £8,741,000).

The Directors declared an interim dividend of 0.69p per share, which was paid on 10 October 2019 (2018: 0.65p per share). The proposed final dividend of 1.76p per share (2018: 1.65p per share) is subject to approval by shareholders at the AGM in May 2020 and has not been included as a liability in these financial statements.

### Capital structure

The Group funds its operations from a number of sources of cash, namely operating cash flow, bank borrowings, finance lease borrowings and shareholders' equity, comprising share capital, reserves and retained earnings. The Group's objective is to achieve a capital structure that results in an appropriate cost of capital whilst providing flexibility in immediate and medium-term funding to accommodate any material investment requirements.

The Company has one class of ordinary share, which carries no right to fixed income. Each ordinary share carries the right to one vote at general meetings of the Company. There are no restrictions on the size of shareholdings nor on the transfer of shares. Both are governed by the Articles of Association and prevailing legislation. The Directors are not aware of any agreements between the Company's shareholders that may result in restrictions on the transfer of securities or on voting rights.

No person has any special rights of control over the Company's share capital and all issued shares are fully paid. Details of the issued share capital and movements during 2019 are shown in note 20.

The Company's banking facilities may, at the discretion of the lender, be repayable on a change of control.

The Company is governed by its Articles of Association, the 2018 UK Corporate Governance Code and the Companies Act 2006 with regard to the appointment and replacement of Directors. The Articles may be amended by special resolution of the shareholders. The powers of the Directors are detailed in the Corporate Governance report.

The Directors will propose an ordinary resolution at the 2020 AGM seeking authority to allot shares in the Company under section 551 of the Companies Act 2006 up to an aggregate nominal amount of £13,151,000.

At the 2019 AGM, the Directors were given authority to allot further ordinary shares, disapplying any pre-emption rights, beyond those committed to the share option schemes or long term incentive plans up to an aggregate nominal value of £3,938,690, which expires at the conclusion of the 2020 AGM. A special resolution will seek to renew for a further year the authority over the existing unissued and uncommitted ordinary share capital of £3,945,300.

### Employees and employee share schemes

The Company's policies for employees and employee engagement are set out in the Corporate Responsibility Report. Option awards are detailed in the Directors' Remuneration Report with those awards outstanding at 31 December 2019 set out in note 26.

## Substantial holdings

	Number of shares held	Percentage
Funds managed or advised by Rights & Issues Investment Trust plc	17,250,000	10.9%
Funds managed by Canaccord Genuity Group Inc.	16,996,325	10.8%
Funds managed or advised by Otus Capital Management	9,917,419	6.3%
Funds managed or advised by Charles Stanley	9,864,735	6.3%
Almadon Limited	9,090,909	5.8%

### Employee share schemes

The Remuneration Committee supervises the award of longer-term share incentives and specifies the performance conditions at the time of the award, having regard to the objectives of the Company and market practice at that time. Further detail is given in the Directors' Remuneration Report.

### Substantial holdings of shares in the Company

The Company has received notification prior to 27 February 2020 in accordance with Rule 5 of the Financial Conduct Authority's Disclosure and Transparency Rules of the voting rights as a shareholder of the Company in the table above.

### Directors

The names of the Directors in office at 31 December 2019 together with short biographical details, are set out on pages 30 and 31. The Board considers its three Non-executive Directors to be independent.

All Directors now retire by rotation at the AGM in May 2020 and offer themselves for re-election. P.D. Atkinson and J. Love have service contracts dated 6 October 2003 and 11 October 1999 respectively, with notice periods of twelve months. S.R. Paterson has a letter of appointment dated 29 September 2017 with a notice period of six months. R. McLellan, J.W.F. Baird and A.M. Dunstan each have letters of appointment dated 10 March 2019, 8 January 2018 and 1 September 2018 respectively, with a notice period of three months.

No Director, either during or at the end of the financial year, had an interest in any contract relating to the business of the Company or any of its subsidiaries. The statement of Directors' interests in the ordinary share capital of Macfarlane Group PLC is contained in the Directors' Remuneration Report on page 36.

There are no agreements between the Company and its Directors or employees that provide for compensation for loss of office or employment that occurs in the event of change of control.

### Directors' and officers' liability insurance

The Company has maintained Directors' and officers' liability insurance cover throughout the financial year. The Company has made qualifying third party indemnity provisions for the benefit of Directors which remain in force.

### Political donations

It is Macfarlane Group's policy not to make donations for political purposes.

### Special business

A special resolution will be put to shareholders to renew for a further year the authority in relation to the disapplication of pre-emption rights over the existing unissued and uncommitted ordinary share capital. This authority is limited to a maximum nominal amount of £3,945,300, representing 10% of the current share capital.

### Disclosure of information to auditor

The Directors holding office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware. Each Director has taken all the steps that they ought to have taken as a Director to make themselves 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.

### Independent auditor

Deloitte LLP were appointed as auditors during the year, following a tender process, described in the Audit Committee report. A resolution to re-appoint Deloitte LLP as the Company's auditor will be proposed at the AGM in 2020.

### Company information

The Company is registered in Scotland (SC 004221) and its registered office is at 3 Park Gardens, Glasgow, G3 7YE.

### Approval

The Strategic Report on pages 4 to 29, which is incorporated within the Directors' Report on pages 4 to 51 were approved by the Board on 27 February 2020.

**Derek L.H. Quirk**  
Company Secretary  
27 February 2020



# Remuneration report

## Remuneration Committee Chair's summary statement

On behalf of the Board, I am pleased to present the Directors' Remuneration Report for the year ended 31 December 2019, which has been drawn up under the provisions of the Enterprise and Regulatory Reform Act 2016 taking into account the new requirements of The Companies (Miscellaneous Reporting) Regulations 2018. In addition to this statement the Directors' Remuneration Report includes the Annual Report on Remuneration on pages 35 to 40. Shareholders will be asked to approve our Directors' Remuneration Report at our AGM in May 2020 as a normal, annual advisory vote. For information, we have also provided a summary of the Remuneration Policy, approved by shareholders at the 2019 AGM, on pages 41 to 43. This does not form part of the Directors' Remuneration Report which shareholders are being asked to approve at our 2020 AGM.

The Company has a Remuneration Committee constituted in accordance with the 2018 UK Corporate Governance Code. The Committee comprises three independent Non-executive Directors plus the Company Chairman. The Committee determines the remuneration for the Executive Directors and also, in consultation with the Chief Executive, determines the total individual remuneration package of his direct reports, setting incentive targets and determining share award levels to ensure a competitive reward is available for key executives within an appropriate governance framework.

### Remuneration in 2019

I am grateful for the support which our shareholders gave on the resolutions to approve our Directors' Remuneration Report for 2018 and the renewed three-year Directors' Remuneration Policy at our 2019 AGM.

The Group results for 2019 are as set out in our Strategic Review. We believe these are appropriately

reflected in the Annual bonus outcomes for 2019 (46% and 41% of maximum; 22.98% and 20.48% of base salary for our two Executive Directors). We have disclosed the performance measures for our 2019 Annual bonus plan on page 35.

In May 2019, we also made our first Performance Share Plan ('PSP') awards since 2015. These were made subject to three year EPS growth targets, which the Committee regards as appropriately stretching. The range of fully diluted EPS before exceptional items of 6.77p to 8.12p, to enable vesting, represent a three-year CAGR range of between 5.8% and 12.5%. In addition, as an underpin, no part of a PSP award will vest unless the Remuneration Committee also considers that Macfarlane's overall performance during the three-year period to 31 December 2021 warrants vesting. These PSP awards from 2019 onwards are subject to a two-year holding period following the initial three-year performance vesting period. Executive Directors hold Macfarlane Group shares worth between 2.5 and 4 times salary at 31 December 2019.

The level of PSP awards in 2019 for our Executive Directors were over shares worth 100% of the Directors' base salaries as permitted by the Directors' Remuneration Policy. The Committee had anticipated making PSP awards at 50% of base salary and included a statement in the 2018 Directors' Remuneration Report to this effect, but after consideration and further review, the Committee determined that PSP awards at 100% of base salary should be made in 2019. The reason for this change of approach was to recognise that these awards were the first PSP awards made since 2015, and accordingly it was considered to be in shareholders' interests to ensure that our Executive Directors are appropriately aligned to shareholders through slightly larger, but still modest PSP awards that directly link potential reward to the

future performance of the Company. Our Chairman consulted with a number of our leading shareholders on this matter before these PSP awards were granted following our AGM in May 2019.

### Remuneration in 2020

The key components of executive remuneration at Macfarlane in 2020 are substantially unchanged from 2019:

- Basic salary and benefits – Base salaries have increased by 2% from 1 January 2020 (2019: 2%) in line with the wider employee population
- Annual bonus – in 2020 there is again a maximum payment opportunity of 50% of salary with 40% of salary based on Profit before tax ('PBT') performance and 10% of salary based on personal objectives. Payment of the personal objectives element of the Annual bonus is subject to achieving a threshold PBT performance. All annual bonus payments are subject to the discretion of the Committee
- Pension – pension contribution levels are unchanged from 2019
- Long term incentives – the Committee's intention is to make further PSP awards in 2020. The level of 2020 PSP awards for Executive Directors will be over shares with a value equivalent of up to 100% of base salaries. Vesting will again be subject to three-year EPS growth conditions with a further underpin vesting condition. Details of the performance conditions for these awards will be set out in the 2020 Directors' Remuneration Report.

I do hope that you will feel able to continue to support the resolution to approve this Directors' Remuneration Report at the AGM in May 2020.

**Andrea Dunstan**  
Chair of the Remuneration Committee  
27 February 2020

## Annual report on remuneration

The details set out on page 35 and 36 of this report have been audited by Deloitte LLP.

### Single total figure of remuneration for each Director

	Salary and fees £000	Taxable benefits £000	Pension costs £000	Fixed pay £000	Bonus £000	Variable pay £000	Total pay £000
<b>2019</b>							
<b>Chairman</b>							
S.R. Paterson	67	–	–	67	–	–	67
<b>Executive Directors</b>							
P.D. Atkinson	355	16	78	449	81	81	530
J. Love	176	9	33	218	36	36	254
<b>Non-executive Directors</b>							
R. McLellan	34	–	–	34	–	–	34
J.W.F. Baird	34	–	–	34	–	–	34
A.M. Dunstan	34	–	–	34	–	–	34
<b>Total</b>	<b>700</b>	<b>25</b>	<b>111</b>	<b>836</b>	<b>117</b>	<b>117</b>	<b>953</b>
<b>2018</b>							
<b>Chairman</b>							
S.R. Paterson	66	–	–	66	–	–	66
<b>Executive Directors</b>							
P.D. Atkinson	348	16	76	440	–	–	440
J. Love	172	8	33	213	–	–	213
<b>Non-executive Directors</b>							
R. McLellan	33	–	–	33	–	–	33
J.W.F. Baird (appointed January 18)	32	–	–	32	–	–	32
A.M. Dunstan (appointed September 18)	11	–	–	11	–	–	11
M. Arrowsmith (retired August 18)	22	–	–	22	–	–	22
<b>Total</b>	<b>684</b>	<b>24</b>	<b>109</b>	<b>817</b>	<b>–</b>	<b>–</b>	<b>817</b>

Taxable benefits relate to provision of a company car (or equivalent allowance) and private medical insurance.

### Directors' pension entitlements

P.D. Atkinson receives a cash allowance which equates to 25% of basic salary, including the related employer's national insurance contributions. J. Love is a member of Macfarlane Group PLC Pension & Life Assurance Scheme (1974) and the basis of his benefits is consistent with all active members of the scheme. His accrued pension at 31 December 2019 was £47,300 (2018: £45,100). The related transfer value was £946,000 (2018: £902,000) calculated using HMRC guidelines. The scheme's normal retirement date is 65 with no automatic entitlement to early retirement.

### Annual bonus for the year ended 31 December 2019

Annual bonus is based on performance against financial targets and personal objectives as set out in the Remuneration Policy. Bonuses are paid in cash following Board approval of the Group Accounts each year. The financial targets for 2019 are shown below:

2019 profit before tax		
Threshold	25% of incentive	£11.75m
Target	50% of incentive	£12.25m
Maximum	100% of incentive	£13.75m
<b>Actual performance</b>		<b>£12.02m</b>
Payout as a % of salary		15.48%

## Remuneration report (continued)

A bonus of up to 10% of base salary is also payable for achievement of personal performance objectives. No bonus is payable under the personal performance element unless the threshold level of PBT, £11.75 million, is achieved. The table below summarises the personal achievements of the Executive Directors.

	Payout	% of maximum
P.D. Atkinson	7.5%	75%
J. Love	5.0%	50%

The total bonus payable for 2019 to P.D. Atkinson was £81,476 (22.98% of salary) and to J. Love was £35,968 (20.48% of salary) respectively.

### Long term incentives for the year ended 31 December 2019

The Company operates a PSP under which shares are awarded which vest subject to performance over a three-year period. There were no outstanding awards due to vest during 2019.

### Grant of 2019 PSP awards

Awards were granted in 2019 over shares worth 100% of salary to each Executive Director, which will vest subject to EPS targets for the financial year ended 31 December 2021. The EPS performance conditions are shown below:

	EPS targets (based on fully diluted EPS before exceptional items)
Threshold (25% of maximum)	6.77p
Maximum (100%)	8.12p

Vesting of the award will also be subject to an underpin assessment by the Remuneration Committee that it must be satisfied regarding overall Company performance before vesting is confirmed. The awards are subject to a two-year post-vesting holding period.

	Awards held at 1 January 2019	Awards granted during the year	Awards exercised during the year	Awards lapsed during the year	Awards held at 31 December 2019
P.D. Atkinson	—	330,123	—	—	<b>330,123</b>
J. Love	—	163,525	—	—	<b>163,525</b>

The 2019 PSP awards were granted at the three-day average share price of 107.4p from the last trading day prior to grant on 17 May 2019. The face value of awards made in the year was £354,552 to P.D. Atkinson and £175,626 to J. Love.

### Payments to past Directors

No payments were made to former Directors in the year or payments made for loss of office.

The shareholdings and share interests of the Directors in office at 31 December 2019 were as set out below:

	2019		2018	
	Beneficial	Options	Beneficial	Options
S.R. Paterson	<b>120,000</b>	—	120,000	—
P.D. Atkinson	<b>854,172</b>	<b>330,123</b>	854,172	—
J. Love	<b>800,000</b>	<b>163,525</b>	800,000	—
R. McLellan	<b>102,819</b>	—	102,819	—
J.W.F. Baird	<b>66,605</b>	—	66,605	—
A.M. Dunstan	<b>10,000</b>	—	10,000	—

Executive Directors are expected to build up a prescribed level of shareholding equivalent to 100% of base salary. Both P.D. Atkinson and J. Love materially exceed these requirements.

Options held by P.D. Atkinson and J. Love are in respect of the PSP awards made in 2019. These are unvested and subject to the achievement of performance targets as described above.

The share price ranged from 73.00p to 109.00p in the year. The closing share price on 31 December 2019 was 107.75p.

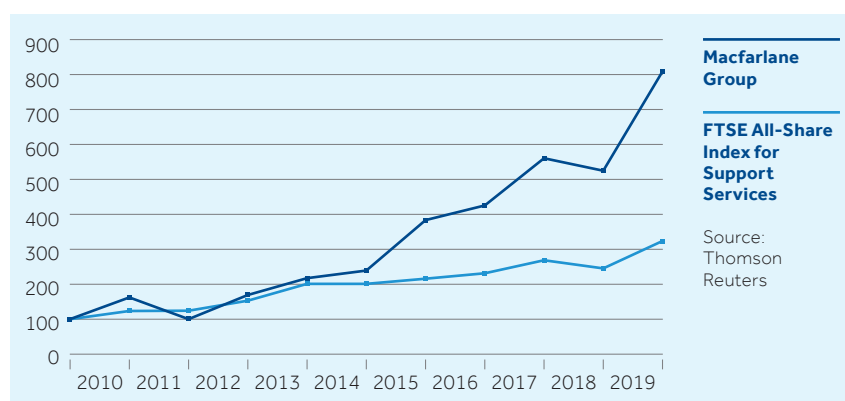


The remainder of the Annual report on remuneration is not subject to audit.

### Performance graph and table

The graph below shows Macfarlane Group's performance, measured by Total Shareholder Return, compared with the performance of the FTSE All-Share Index for Support Services, also measured by Total Shareholder Return for the period since 1 January 2010. The Index for Support Services has been selected because it includes a range of companies, which the Remuneration Committee considers to be the best available comparison to Macfarlane Group for this purpose.

### Total shareholder return index



### CEO single figure

		Fixed remuneration £000	Variable remuneration £000	Single figure of total remuneration £000	Annual variable element award vs. maximum opportunity	Long term incentive vesting against maximum opportunity
2019	P.D. Atkinson	449	81	530	46%	n/a
2018	P.D. Atkinson	440	0	440	0%	n/a
2017	P.D. Atkinson	433	81	514	48%	0%
2016	P.D. Atkinson	424	92	516	55%	n/a
2015	P.D. Atkinson	416	92	508	56%	n/a
2014	P.D. Atkinson	408	178*	586	46%	n/a
2013	P.D. Atkinson	400	16	416	10%	n/a
2012	P.D. Atkinson	392	70	462	45%	n/a
2011	P.D. Atkinson	400	15	415	10%	n/a
2010	P.D. Atkinson	396	15	411	10%	n/a

\* This includes £105k in respect of the exercise of options which vested in 2007.

### Percentage change in remuneration of CEO and employees

The table below shows the % change in remuneration from 2018 to 2019 for the CEO and all Group employees.

Change in	CEO	Average for all eligible Group employees
Base salary	2.0%	2.0%
Benefits	0.0%	11.0%
Bonus	100.0%	82.5%

No bonus was paid to the CEO in 2018 hence the level of change.

## Remuneration report (continued)

### Relative importance of spend on pay

The difference in expenditure between 2018 and 2019 on remuneration for all employees in comparison to the distribution to shareholders by way of dividend is set out below:

	2019 £000	2018 £000	Change
Total employee pay	30,311	27,791	+9.1%
Dividend	3,689	3,387	+8.9%

### CEO to employee pay ratio

The table below shows the ratio of total remuneration for the CEO to that of the lower quartile, median and upper quartile paid employee.

Financial year	Method	25th percentile pay ratio	50th percentile pay ratio	75th percentile pay ratio
2019	Option B	24.6 : 1	18.9 : 1	16.4 : 1

### Notes to CEO to employee pay ratio

Option B, using the gender pay gap reporting data to identify the individuals who represent the three quartiles, was chosen as the methodology as this data was readily available on a Group-wide basis.

Total remuneration for the CEO and for the individuals who represent the three quartiles was determined for the year to 31 December 2019. The three individuals are all full-time employees and are considered to be representative of the 25th percentile, median and 75th percentile pay levels in the Company.

The median pay ratio is reflective of Macfarlane's approach, including our policy of not paying excessive salaries to Executive Directors. There was no PSP award vesting in the year, which resulted in a lower ratio than would otherwise have been the case.

The table below shows the total pay and benefits and the salary component of total pay for the three quartiles.

Financial year	Salary component of total pay and benefits			Total pay and benefits		
	25th percentile	50th percentile	75th percentile	25th percentile	50th percentile	75th percentile
2019	£18,585	£26,998	£30,600	£21,554	£28,078	£32,324

### Statement of implementation of remuneration policy in 2020

The salaries of the Chief Executive and the Finance Director were increased by 2.0% to £361,644 and £179,143 respectively with effect from 1 January 2020, which is in line with the average increase for the Group's workforce. Fees paid to the Chairman and Non-executive Directors also increased by 2.0% to £68,931 and £34,465 respectively from 1 January 2020.

There are no changes proposed to the operation of benefits and pensions from the bases operated in 2019.

Executive Directors will be eligible to receive an annual bonus of up to 50% of base salary, with 40% of salary based on PBT targets and 10% of salary based on personal objectives. No element of the annual bonus is payable if the PBT threshold target is not achieved. The precise targets are considered by the Board to be commercially sensitive at this time, but will be disclosed in next year's Directors' Remuneration Report.

The Remuneration Committee intends to make awards under the PSP based on the following principles:

- An annual award over shares with a face value of up to 100% of salary (within the existing 100% of salary limit);
- A fixed three year performance period (with no re-testing);
- A two year post-vesting holding period;
- A performance condition based on Earnings per share performance with a 25% threshold level for vesting and subject also to an 'underpin' assessment by the Remuneration Committee that it must be satisfied regarding overall Company performance before vesting is confirmed; and
- The precise targets will be set by the Committee at the time of the award and will be disclosed in next year's Directors' Remuneration Report.

### Details of the Remuneration Committee, advisers to the Committee and their fees

The Remuneration Committee currently comprises three independent Non-executive Directors and the Company Chairman. Details of the Directors who were members of the Committee during the year are disclosed on page 47.

The Remuneration Committee used the services of FIT Remuneration Consultants LLP to advise on certain aspects of remuneration during 2019 and fees of £12,597 were charged for the year for that advice. The Directors consider FIT Remuneration Consultants LLP to be independent of the Group and objective in their advice.

### Remuneration Committee's reporting obligations

The Remuneration Committee considered its obligations under the 2018 UK Corporate Governance Code and concluded that:

- The Directors' Remuneration Policy, as approved by shareholders in May 2019, and our implementation of the Policy (including the use of PBT and personal performance measures for the Annual bonus and EPS performance measures for the PSP) support the Company's strategy.
- The use of PBT and EPS measures reflect the Company's focus on growing profits and our aims of paying an attractive level of dividend balanced against the need to retain funds in the business to finance growth, make pension contributions, fund acquisitions and meet capital expenditure requirements.
- Remuneration for the Executive Directors remains appropriate and consistent with our policy of not paying excessive salaries. The Remuneration Policy operated as intended in the year, with our Annual bonus plan delivering 46% of the maximum bonus opportunity to our Chief Executive in the year. This reflects another strong year for Macfarlane Group in which we exceeded the PBT threshold, although performance fell short of the maximum stretch level. The maximum stretch targets are deliberately set at challenging levels so as to reward only truly exceptional performance.

In addition, the Committee addressed the six factors outlined in Provision 40 of the 2018 Code when determining the Executive Directors' remuneration.

- **Clarity** – Our Policy is well understood by the Executive Directors and by our shareholders, with whom we engaged when revising the Policy last year.
- **Simplicity** – The Remuneration Committee is conscious that overly complex remuneration structures are less impactful than simple structures and has strived to keep Executive Directors' pay as simple as possible whilst also offering a competitive remuneration package.
- **Risk** – Our Policy has been designed to ensure that it does not promote excessive risk taking (for example, the annual bonus and PSP operate on sliding performance scales, rather than relying on binary performance targets) and prevents 'payment for failure' through modest fixed remuneration and the use of stretching financial performance targets. The PSP, which forms the majority of variable pay opportunity, is delivered in shares which vest after three years, with a further two-year holding period, ensuring a link to sustained, long-term performance.

Malus and clawback apply to both the annual bonus and the PSP.

- **Predictability** – Incentive plans for our Executive Directors are subject to individual and overall caps, ensuring that the Remuneration Committee has control over levels of reward. The weighting of variable pay opportunity towards the PSP means that actual pay outcomes are highly aligned to the experience of our shareholders.
- **Proportionality** – All pay levels are appropriately proportionate, not excessive and reflect Macfarlane Group's outlook and culture. Executive Directors' fixed remuneration is set, after consideration of external benchmarks, at a level that is competitive but affordable for Macfarlane Group, with variable pay linked to the achievement of stretching performance targets.
- **Alignment to culture** – The performance targets which are used to measure both the annual bonus and the PSP are stretching, consistent with Macfarlane Group's performance-led culture. We do not believe that variable pay should be paid for poor performance and have a long track record of setting robust performance targets.

The Remuneration Committee receives a report on pay and benefits across the Company which it considers when setting remuneration for Executive Directors. While employees are not directly consulted when setting Executive Directors' remuneration, Andrea Dunstan acts as designated Non-Executive Director for employee engagement in addition to her role as Remuneration Committee Chair, and so the Remuneration Committee is fully updated on any views on remuneration which arise from the engagement process.

Whenever the Board has engaged with shareholders during the year, it has received generally positive feedback, including on remuneration matters.

## Remuneration report (continued)

### Statement of voting at the Annual General Meeting on 14 May 2019

The Directors' Remuneration Report received the following votes from shareholders.

	Total number of votes	% votes cast
For	55,236,967	87.14%
Against	8,154,946	12.86%
<b>Total votes cast (for or against)</b>	<b>63,391,913</b>	100.00%
Votes withheld	227,393	
<b>Total</b>	<b>63,619,306</b>	

The Directors' Remuneration Policy received the following votes from shareholders.

	Total number of votes	% votes cast
For	58,469,089	91.98%
Against	5,101,010	8.02%
<b>Total votes cast (for or against)</b>	<b>63,570,099</b>	100.00%
Votes withheld	49,207	
<b>Total</b>	<b>63,619,306</b>	

Votes received on 14 May 2019 (including votes withheld) amounted to 40.38% of the issued share capital.





## Remuneration policy

Pages 41 to 43 detail the principal features of the Directors' Remuneration Policy approved at the 2019 AGM, which is shown in full under the Corporate Governance section of the Group website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)).

### Salary (fixed pay)

Link to strategy	Pay a fair salary commensurate with the individual's role, responsibilities and experience and having regard to market rates for similar roles in comparable companies.
Operation	The Committee reviews base salaries annually with changes effective from 1 January. This review takes into account practices elsewhere in the Group. Salary is pensionable.
Opportunity	There is no prescribed maximum salary or maximum rate of increase. The Committee takes into consideration the general increase for the broad employee population but on occasion may recognise changes in responsibility, development in the role or specific retention issues.

### Retirement benefits (fixed pay)

Link to strategy	Provide competitive pension arrangements to aid recruitment/retention of senior executives.
Operation	The Group pays a pension allowance or contributes to a pension scheme for Executive Directors. The Group's legacy defined benefit scheme has been closed to new members since 2002 and the pensionable salary frozen in 2010. Pension contributions for new appointments will be kept under review in line with developing market practice.
Opportunity	Company contribution of up to 25% of base salary or equivalent cash allowance in lieu (inclusive of employer's national insurance contribution) are currently paid.

### Other benefits (fixed pay)

Link to strategy	Provide cost effective benefits to aid recruitment and retention of senior executives and to support the wellbeing of employees.
Operation	Benefits include, car allowance or company car, private medical insurance, permanent health insurance and any other such benefits as the Committee considers appropriate.
Opportunity	The benefits are not subject to a specific cap but represent a small element of total remuneration. Costs to provide these benefits are closely monitored.

### Annual bonus (variable pay)

Link to strategy	Incentivise performance over a 12 month period based on the attainment of financial targets and individual performance objectives agreed by the Remuneration Committee.
Operation	The bonus is paid in cash based on the audited financial results and the Committee's assessment of delivery against personal objectives. Bonus awards are subject to malus and clawback provisions for 2 years following the award.
Opportunity	Maximum bonus potential capped at 100% of base salary but remains at 50% for 2019. The Annual bonus is not pensionable.
Performance measures	Performance measures may be financial or non-financial and corporate, divisional or individual and in such proportions as the Committee considers appropriate. The annual bonus plan remains a discretionary arrangement and the Committee retains a standard power to apply judgement to adjust the outcome of the plan for any performance measure (from zero to any cap) should it consider that to be appropriate.

## Remuneration policy (continued)

### Long term incentives (variable pay)

Link to strategy	Incentivise delivery of strategic targets and sustained performance over the long-term.
Operation	<p>Conditional awards over shares may be granted each year, which can be earned subject to delivery of performance goals. The Committee will set such performance conditions on PSP awards as it considers appropriate (whether financial or non-financial and corporate, divisional or individual). These conditions are for a fixed 3 year period with no re-testing.</p> <p>Executive Directors are expected to build up a prescribed level of shareholding equivalent to 100% of base salary. If the prescribed shareholding has not been reached, Executive Directors will be expected to retain a proportion of the shares vesting under the Company's PSP until the guideline is met.</p> <p>LTIP awards are subject to malus and clawback provisions for 3 years following vesting.</p>
Opportunity	Awards are capped at a maximum of 100% of base salary in normal circumstances (200% in exceptional circumstances).
Performance measures	Conditional awards will vest based on three-year performance against challenging financial and other targets set and assessed by the Committee in its discretion.

### Clawback/malus in the Annual bonus and long term incentives

Provisions are in place for both Annual bonus and LTIP arrangements to operate malus and/or clawback in certain exceptional circumstances, including the material misstatement of the Company's results (annual bonus and LTIP), if the assessment of performance on which vesting is based was based on an error (LTIP only) or circumstances which would warrant the summary dismissal of the individual, whether or not the Company has chosen to do so.

### Consideration of employment conditions elsewhere in the Group

There is a periodic employee survey and the Board receives a regular presentation from the Director of Human Resources, which includes consideration of the Group's remuneration policies. As a result, the Remuneration Committee has not conducted a specific employee consultation exercise on the Directors' remuneration policy.

While appropriate benchmarks vary by role, the Company seeks to apply the philosophy behind this policy across the Group as a whole. Where the Company's pay policy for Directors differs from its pay policies for groups of employees, this reflects the appropriate market rate position and/or typical practice for the relevant roles. The Committee takes into account pay levels, bonus opportunity and share awards across the Group when setting the Remuneration Policy.

### Consideration of shareholder views

The Committee considers shareholder feedback received as part of any dialogue with shareholders via the Chairman, executive management or the Company's brokers. Where necessary the Remuneration Committee Chair will engage pro-actively with shareholders such as in advance of proposed awards under the Performance Share Plan.

### Approach to recruitment remuneration

The Remuneration Committee will follow the above policy when setting remuneration for a new Executive Director. Base salary will be set at a competitive level appropriate for the role and experience of the Director being appointed. In the case of an external appointment, the Committee may consider it appropriate to recognise awards or benefits that will or may be forfeited on resignation from the previous appointment. This may be cash and/or share awards but the maximum payment will be no more than the Committee considers is required to provide reasonable compensation.

If the Director is required to relocate then reasonable relocation, travel and subsistence payments will be provided at the discretion of the Committee and for a period of no more than two years following appointment.

### Service contracts and letters of appointment

Executive service contracts have a standard notice period of 12 months. The Committee reserves flexibility to alter these principles to secure the appointment of an appropriate candidate and if appropriate introduce a longer initial notice period, of up to two years, reducing over time. Executive Directors may accept appointments outside the Company provided the Board's permission is obtained, however the Board may require the fees from these appointments to be accounted for to the Company. Neither P.D. Atkinson nor J. Love currently hold any external appointments.

Chairman and Non-Executive Director appointments are made using letters of appointment for periods not exceeding three years subject to re-election at the AGM and contain notice periods of six months and three months respectively.

### Non-executive Director remuneration policy

#### Chairman

Link to strategy	To attract and retain a high-calibre Chairman by offering a market competitive fee level.
Operation	The Chairman is paid a single fee for all his responsibilities, which is reviewed periodically by the Committee with reference to other comparable companies.
Opportunity	The current fee is £68,931 and is subject to periodic change under this policy. There is no maximum fee level.

#### Non-executive Directors

Link to strategy	To attract and retain high-calibre Non-executive Directors by offering a market competitive fee level.
Operation	Non-executive Directors are paid a basic fee. Committee Chairs may be paid a supplement to reflect additional responsibilities. Fee levels are reviewed periodically by the Chairman and the Executive Directors with reference to other comparable companies.
Opportunity	The current fee is £34,465 and is subject to periodic change under this policy. There are currently no supplementary fees paid and there is no maximum fee level.

### Payment for loss of office

The Committee's policy for an Executive Director whose employment is to be terminated is to agree a termination payment based on the value of base salary, contractual pension contributions and other benefits that would have accrued during the contractual notice period unless there has been a breach of the service agreement by the Director.

The policy is that the departing Director may work or be placed on garden leave for all or part of their notice period or receive payment in lieu of notice in accordance with the service agreement. The Committee supports the principle of mitigation and phased payments relative to any settlement and will take legal advice in relation to any settlements to be proposed. Share-based entitlements for Executive Directors will be determined based on the relevant plan rules.

The Company has the power to enter into settlement agreements with Directors and to pay compensation to settle potential legal claims. This policy does not include an explicit cap on the cost of termination payments.

### Committee discretions

The Committee has discretion, consistent with market practice, including the terms and the termination of any contract, in relation to the operation and administration of share plans. Any use of these discretions would be explained in the Director's Remuneration Report and if appropriate be the subject of consultation with major shareholders. The Committee may make minor amendments to the policy set out above without obtaining shareholder approval.



## Corporate governance

The Company is committed to the principles of corporate governance set out in the Financial Reporting Council's ('FRC'). UK Corporate Governance Code issued in 2018 ('the Code'). The Company's compliance is set out in the narrative statement on pages 44 to 51 and for Directors' remuneration in the Directors' Remuneration Report on pages 34 to 43.



**Stuart R. Paterson**  
Chairman

### Compliance

The Company fully complied with all the Code provisions during 2019.

The Company's auditor, Deloitte LLP, is required to review whether the above statement (in addition to its wider remit under the Listing Rules) reflects the Company's compliance with the provisions of the Code specified for its review by the Financial Conduct Authority's Listing Rules and to report if it does not reflect such compliance.

### The Board

The current Board structure is in compliance with the Code, requiring companies outside the FTSE 350 to have at least two independent Non-executive Directors.

The Board comprises the Chairman, three independent Non-executive Directors and two Executive Directors. Their names and biographical details, illustrating their range of experience and the benefit that each Director's appointment brings to Macfarlane Group are set out on pages 30 and 31. The Directors believe that the Board has an appropriate independent Non-executive Director complement with recent and relevant experience, which brings strong, independent judgement to the Board's deliberations. Non-executive Directors contribute towards and challenge Group strategy as well as scrutinising performance in meeting agreed objectives and monitoring the reporting of performance. They satisfy themselves as to the integrity of the financial information and that the financial controls, systems of risk management and the Group's governance structure are robust and defensible.

Non-executive Directors are given access to independent professional advice at the Group's expense, subject to certain limits and procedures, when it is deemed necessary in order for them to effectively fulfil their responsibilities.

Details of Executive Directors' service contracts are given in the Directors' Report with both Executive Directors' service contracts having notice periods of one year.

The Company has maintained Directors' and officers' liability insurance cover throughout the financial year. The Company made qualifying third party indemnity provisions for the benefit of Directors in 2009, and these have remained in force throughout 2019 and to the time of this report.

The Board confirms that it has considered and authorised any conflicts or potential conflicts of interest in accordance with the Group's existing procedures.

The Chairman's other commitments are included in his biography on page 30. The Board is satisfied that these do not interfere with the performance of Group duties, which is based on a commitment of approximately 45 days per annum.

The Board considers its Non-executive Directors, Bob McLellan, James Baird and Andrea Dunstan to be independent both in character and judgement. None of these Directors:

- Has been an employee of the Group within the last five years;
- Has, or has had within the last three years, a material business relationship with the Group;
- Receives remuneration other than a Director's fee;
- Has close family ties with any of the Group's advisers, Directors or senior employees;
- Holds cross-directorships or has significant links with other Directors through other companies or bodies;
- Represents a significant shareholder; or
- Has served on the Board for more than nine years from the date of their first election.



The balance of the Board's skills and experience is kept under regular review. The Board's succession plans recognise the need to consider diversity within the Group and in Board composition in the medium-term. We are also committed to improving the sustainability both of our operations and of the products that we offer our customers. The Board recognises that both of these objectives are to the benefit of all stakeholders of the Group.

### **The roles of the Chairman and Chief Executive**

The division of responsibilities between the Chairman and the Chief Executive is very clearly defined and has been approved by the Board. The Chairman is responsible for running the Board, ensuring that all Directors receive sufficient and relevant information on financial, business and corporate issues prior to meetings to allow Directors to bring independent judgement to bear on all issues. The Chairman facilitates the effective contribution of Non-executive Directors and ensures effective communication channels with shareholders. The Chief Executive's responsibilities focus on managing the business and implementing the Group's strategy.

### **Senior Independent Director**

Bob McLellan is the Senior Independent Director. Shareholders may contact him directly if they feel their concerns are not being addressed and resolved through existing mechanisms for investor communication.

### **Re-election of Directors**

At the 2020 AGM, all Directors fall due to retire and, being eligible, offer themselves for election. Directors' service contracts and letters of appointment will be available for shareholder review prior to the AGM on 12 May 2020.

Subject to the Company's Articles of Association, the Companies Act and satisfactory performance evaluation, Non-executive Directors are appointed for an initial period of three years. Before the third and sixth anniversary of the Non-executive Director's first appointment, the Chairman will discuss with the Director whether it is appropriate for a further three-year term to be served.

### **Company Secretary**

Derek Quirk, the Company Secretary, is responsible for advising the Board through the Chairman on all matters relating to corporate governance. Under the direction of the Chairman, the Company Secretary's responsibilities include ensuring good information flows within the Board, its committees and between executive management and Non-executive Directors. The Company Secretary also facilitates induction and assists with professional development for the Board. All Directors have access to the advice and services of the Company Secretary.

The Articles of Association and the schedule of matters reserved for the Board provide that the appointment and removal of the Company Secretary is a matter for the Board as a whole.

### **Board procedures**

The Group is controlled by the Board of Directors. The Board's main roles are to set the Group's strategic objectives, guide and support executive management in achieving these objectives, create value for and safeguard the interests of all shareholders within the appropriate legal and regulatory framework. The Board met seven times during 2019 and individual attendance at those and the Board Committee meetings is set out in the table on the following page. In 2019, three Board meetings were held at operational locations to allow the Board to meet management teams and further develop their understanding of the Group.

The Board has a formal schedule of matters reserved for its approval. The specific matters reserved for the Board include setting the Group's strategy and approving an annual budget, reviewing management performance, approving acquisitions, divestments and major capital expenditure, monitoring returns on investment, reviewing the Group's systems of internal control and risk management and consideration of significant financing matters. The Board has delegated to executive management responsibility for the development and recommendation of strategic plans for consideration by the Board, the implementation of the strategy and policies of the Group as determined by the Board, the delivery of the operating and financial plan, approval of capital expenditure below Board authority levels and the development and implementation of risk management systems.

Board agendas are set by the Chairman, who consults with the Chief Executive and discusses the agendas with the Company Secretary. A programme of areas for discussion is maintained by the Company Secretary to ensure that all matters reserved for the Board and any other key issues are addressed at the appropriate time.

## Corporate governance (continued)

At each meeting, the Directors receive management information and reports from the Chief Executive and the Finance Director which, together with other papers, enables them to scrutinise the Group and management performance against agreed objectives. These and other regular reports and papers are circulated to the Directors in a timely manner in preparation for Board and Committee meetings and are supplemented by information specifically requested by the Directors from time to time.

### Accountability

The Board is responsible for presenting a fair, balanced and understandable assessment of the Group's position and prospects and asks the Audit Committee to consider and advise the Board of its view.

The Board considers that the Annual Report provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

After making the enquiries set out on page 65, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for at least the next twelve months from the date of this report. For this reason they continue to adopt the going concern basis in preparing the financial statements.

The Directors' Responsibilities Statement is set out on page 40.

### Board and Committee meetings

The number of regular Board and Committee meetings attended by each member during 2019 is shown in the table below.

### Professional development

On appointment, Directors complete an induction programme designed to give them a thorough understanding of the Group and its activities. They receive information about the Group, the matters reserved for the Board, the terms of reference and membership of the Board Committees, and the latest financial information. This is supplemented with visits to key locations and meetings with and presentations from senior management.

### Board performance evaluation

The Board has established a formal process, led by the Chairman, for an annual performance evaluation of the Board, its Committees and individual Directors. All Directors are made aware that their performance will be subject to regular evaluation. The Board has completed a self-assessment questionnaire developed to take account of the areas identified in the FRC 'Guidance on Board Effectiveness'. This includes specific reference to strategic objectives and the performance and processes of the Board and all Board Committees. The results are collated by the Company Secretary and reviewed by the Board to identify any areas for improvement

and to confirm objectives for the year ahead. The Chairman then holds individual meetings with each Director to review performance and set individual objectives.

The Chairman meets periodically with the Non-executive Directors without the Executive Directors present. The three Non-executive Directors conduct an annual performance evaluation of the Chairman.

### Relationships with shareholders

The Group maintains a corporate website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)) containing a wide range of information of interest to institutional and private investors.

Detailed reviews of the performance and financial position are included in the Strategic Report on pages 6 to 29 of this report. The Board uses this, together with the Chairman's Statement on pages 4 and 5 and the remainder of the Report of the Directors, to present its assessment of the Company's position and prospects.

The Chairman seeks to maintain a regular dialogue with shareholders and gives feedback to the Board on issues raised. The Group has regular discussions with institutional shareholders, including meetings led by the Chief Executive and the Finance Director, following the announcement of the annual results in February and the interim results in August. Individual requests for discussions from shareholders are considered.

## Attendance by Directors at Board and Committee meetings during 2019

		Board	Audit Committee	Remuneration Committee	Nominations Committee
<b>Stuart Paterson</b>	Chairman	7 (7)	6 (6)*	4 (4)	3 (3)
<b>Peter Atkinson</b>	Chief Executive	7 (7)	—	—	—
<b>John Love</b>	Finance Director	7 (7)	—	—	—
<b>Bob McLellan</b>	Senior Independent Director	7 (7)	5 (6)	4 (4)	3 (3)
<b>James Baird</b>	Non-executive Director	7 (7)	6 (6)	4 (4)	3 (3)
<b>Andrea Dunstan</b>	Non-executive Director	7 (7)	6 (6)	4 (4)	3 (3)

Figures in brackets indicate the maximum number of meetings in 2019 for which the individual was a Board or Committee member. Where a Director cannot attend a Board or Committee meeting, any comments the Director has on the papers being reviewed at that meeting are relayed in advance for consideration.

\* The Chairman attends but is not a member of the Audit Committee.

The Board receives feedback on shareholder meetings including broker feedback for the meetings scheduled around the two results' announcements. The Senior Independent Director is available to meet with shareholders if they have concerns with contact through the normal channels of Chairman, Chief Executive or Finance Director.

All Directors attend the AGM and all shareholders have an opportunity to raise questions with members of the Board on matters relating to the Group's operations and performance during the meeting and to meet Directors after the formal proceedings have ended. Details of the resolutions to be proposed at the AGM can be found in the Notice of Meeting accompanying the Annual Report and Accounts. The Notice of Meeting is sent out more than 20 days in advance of the meeting. In line with the requirements of the Code, the results of proxy votes are disclosed at the AGM, notified to the Stock Exchange and made available on the Group website following the meeting.

### Nominations Committee

The Nominations Committee during 2019 was as follows:

Stuart Paterson (Chair)  
Bob McLellan  
James Baird  
Andrea Dunstan

The Nominations Committee met 3 times during 2019 and its terms of reference are available on the Group website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)).

The principal work undertaken by the Nominations Committee in 2019 was to consider and recommend that the Company propose for re-election any Directors falling due for re-appointment at the AGM.

The Committee's ongoing responsibilities include reviewing the structure, size and composition of the Board and giving full consideration to succession planning for both executive and Non-executive Directors and other senior executives. The Nominations Committee will continue to consider the mix of skills and experience that the Board requires and seek the appointment of Directors to meet its assessment of what is required to ensure that the Board is effective in discharging its responsibilities.

Following a Nominations Committee held on 21 February 2019 the Committee proposed Bob McLellan and John Love for re-election at the AGM on 14 May 2019.

No Director is involved in any decisions regarding their own appointment or re-appointment.

### Remuneration Committee

The Remuneration Committee during 2019 was as follows:

Andrea Dunstan (Chair)  
Bob McLellan  
James Baird  
Stuart Paterson

None of the members of the Remuneration Committee during 2019 has any personal financial interests, other than as a shareholder, in the matters to be decided, conflicts of interests arising from cross-directorships or any day-to-day involvement in running the business.

The Remuneration Committee met 4 times during 2019 and its terms of reference are available on the Group website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)).

The principal work undertaken by the Remuneration Committee in 2019 was:

- (a) To review performance against 2019 financial and personal objectives and to conclude on the appropriate performance related reward under the Annual bonus plan for senior executives including the Executive Directors;
- (b) To approve the financial and personal objectives for 2020 in relation to the performance related Annual bonus plan;
- (c) To consider awards of share-based incentives using the PSP and determining the performance conditions for these awards; and
- (d) To approve the Directors' Remuneration Report.

The work of the Remuneration Committee is described within the Directors' Remuneration Report on pages 34 to 43.

## Corporate governance (continued)

### Audit Committee

During 2019 the Audit Committee comprised:

James Baird (Chair)  
Bob McLellan  
Andrea Dunstan

James Baird was appointed as Chair of the Committee on 8 January 2018 given his relevant experience. The remaining Committee members, Bob McLellan and Andrea Dunstan have a wide range of commercial experience as evidenced in their biographical details on pages 30 and 31. The Company Chairman attends meetings to give the benefit of his relevant experience but is no longer a member of the Committee.

The Committee Chairman will be available to answer questions on any aspect of the Committee's work at the AGM.

The Committee's terms of reference are displayed on the Group website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)) and its principal oversight responsibilities cover the following five areas:

#### • Internal control and risk management

The Committee reviews annually the Group's system of risk management and internal control and processes for evaluating and monitoring the risks facing the Group. The overall responsibility for the systems of internal control and for reviewing their effectiveness rests with the Board.

#### • Internal audit

The Committee monitors and reviews the effectiveness of the Company's internal audit function and its terms of reference annually and recommends to the Board any changes required following the review. Reports from internal audit are considered at each meeting and the Committee actively engages in selecting areas to be audited.

#### • Whistle-blowing

The Committee monitors the Group's arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting and other areas including an external whistle-blowing service to take calls from employees.

#### • External audit

The Committee is responsible for monitoring the effectiveness of the external audit process and making recommendations to the Board on the appointment, re-appointment and remuneration of the external auditor. It is responsible for ensuring that an appropriate relationship between the Group and the external auditor is maintained, including formal consideration of the independence of the external auditor. The Committee considers the framework for the supply of non-audit services by the external auditor and reviews non-audit services and fees.

#### • Financial reporting

The Audit Committee monitors the integrity of the Group's financial statements and the significant judgements contained therein including assessing the fair, balanced and understandable presentation within the reporting. The Committee also considers any other formal announcements relating to the Group's performance. Further details are set out on the following pages.

The Audit Committee met six times during 2019 and its agenda is linked to events in the Group's financial calendar. The Committee meets privately with the external auditor, with internal auditors and Executive Directors invited to attend meetings as required. In 2019 the Audit Committee discharged its responsibilities by:

- Reviewing its terms of reference;
- Reviewing the Group's draft financial statements and interim results statement prior to Board approval and reviewing the external auditor's reports on the final results and draft financial statements;
- Debating the continuing appropriateness of the Group's accounting policies;
- Monitoring compliance with International Financial Reporting Standards;
- Challenging the output from the Group-wide process used to identify, evaluate and mitigate risks and associated mitigating controls;
- Reviewing the effectiveness of the Group's internal controls and disclosures made in the Annual Report;
- Reviewing the effectiveness of the previous external auditor at the conclusion of the 2018 audit;
- Agreeing the programme of work for the internal audit function taking into account identified risks;
- Discussing reports from the Head of Internal Audit on internal audit reports and management responses to proposals made in these reports, ensuring that the responses are actioned and completed on a timely basis;
- Reviewing the Group's tax risk strategy and risk management policy before publication on the Group website;
- Conducting an audit tender process resulting in the appointment of Deloitte LLP as the new external auditors;
- Agreeing the external auditor's plan for the audit of the Group accounts which includes confirmations of auditor independence and approval of the engagement letter; and
- Reviewing and approving the external audit fee and keeping the level of non-audit fees under review.



Following each Audit Committee meeting, copies of the minutes of the meetings are circulated to all Board Directors and are made available to the external auditors by the Company Secretary, who acts as Secretary to the Committee.

### 2019 financial statements

Certain accounting policies require key accounting judgements or involve particularly complex or subjective estimates or assumptions which will have a significant effect on the amounts recognised in the financial statements. The Audit Committee receives a report from the Finance Director for each reported set of results, which summarises principal judgements taken by executive management. The Committee discusses and challenges these judgements and considers the report together with the results of the external audit. The Committee then makes a recommendation to the Board on the suitability of the policies and judgements supporting the reported results.

For the 2019 financial statements, the Committee considers the two most significant areas of judgement to be:

#### Pension scheme deficit

A net liability is recorded at each reporting date equivalent to the deficit on the Group's defined benefit pension scheme. This liability is determined in conjunction with advice from the pension scheme actuary and can fluctuate significantly based on a number of assumptions, some of which are linked to market-related factors outwith the control of management. The main actuarial assumptions that impact the deficit are set out in note 25. Investments are valued at bid price.

The Audit Committee has debated the assumptions being used to determine the liabilities in accordance with guidance from a number of actuarial firms and has satisfied itself that the assumptions used fall within an acceptable range reflecting the duration of liabilities in Macfarlane Group's defined benefit pension scheme.

The pension scheme deficit calculated by the actuary and the related disclosures are based on these assumptions and the components of the movement in the deficit in 2019 have been explained to the Committee's satisfaction. The sensitivities of movements in the key underlying assumptions are clearly set out in note 25. Accordingly the Committee is comfortable with the reporting of the pension scheme deficit.

#### Valuation of trade receivables

Trade receivables recorded in the Group's balance sheet comprise a large number of individual balances. The Group reviews all trade receivables and provides against potentially irrecoverable items throughout the year, applying an expected credit loss model. The Group's executive management then reviews local judgements. Whilst every attempt is made to ensure that the provision held against doubtful trade receivables is as accurate as possible, there remains a risk that the provision may not match the level of debt, which ultimately proves uncollectible. At 31 December 2019, the Group retained a provision held against trade receivables of £310,000 (2018: £304,000) as set out in note 15.

The Audit Committee receives details of individual receivables greater than £25,000 twice in each year. The Committee reviews the extent to which year-end balances have been settled in 2020 to date, paying particular attention to receivables outwith terms and any bad debts written off, comparing this with similar analyses produced at previous reporting dates. This is then considered against the level of provision held against trade receivables. Based on this analysis, the Committee is of the view that the level of provision and the disclosures of items beyond terms is appropriate.

### Consideration of other matters

The Committee debates a number of other areas for each reporting period, but does not consider these matters to be of such significance as those above. For the 2019 financial statements, the main other areas included:

- The acquisition of subsidiaries is accounted for under the acquisition method. Acquired businesses are measured at the date of acquisition as the aggregate fair value of assets, liabilities and contingent liabilities. The excess of the cost of acquisition over the fair value of the identifiable net assets is classified as goodwill. The Committee reviews this process for each acquisition undertaken and discusses the methodology and assumptions used with management. The Committee concluded that it was satisfied with the basis of accounting in this area and the resulting measurements;
- Goodwill is allocated to cash generating units ('CGUs') expected to benefit from the synergies of the business combination, for the purpose of impairment testing. Carrying values of goodwill for each CGU grouping are considered annually. The Committee reviews and discusses management's approach to impairment testing including the related sensitivity analysis. The Committee was satisfied with the assumptions and judgements applied, concluding that there was no evidence of impairment of goodwill;
- Reviewed the process for accumulating information and the disclosures of information on the adoption of IFRS 16 'Leases' on 1 January 2019 and subsequent year-end reporting;
- The level of and basis for inventory provisions at 31 December 2019;
- A review of the viability statement including disclosure of the terms of the Group's banking facilities; and
- Disclosure of Alternative Performance Measures ('APMs') in relation to the exceptional costs in 2018.

## Corporate governance (continued)

### Audit Committee (continued)

For all of these other matters the Audit Committee is satisfied with the approach taken.

The Audit Committee has reviewed the contents of this year's Annual Report and Accounts and has advised the Board that, in its view, the report is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy.

The Committee monitors the Group's arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting and other areas including an external whistle-blowing service to take calls from employees. Details of the arrangements are on the Group website ([www.macfarlanegroup.com](http://www.macfarlanegroup.com)). All concerns are investigated at the earliest opportunity and the employee's anonymity preserved wherever possible.

### Relationship with external audit

The Audit Committee is responsible for the development, implementation and monitoring of the Group's position on external audit. The Committee's terms of reference assign oversight responsibility for monitoring the independence, objectivity and compliance of the external auditors with ethical and regulatory requirements to the Audit Committee, and day-to-day responsibility to the Finance Director. The Audit Committee ensures that the Board and external auditor have safeguards in place to prevent auditor's independence and objectivity being compromised. The external auditor also reports to the Committee on the actions that it has taken to comply with professional and regulatory requirements and current best practice in order to maintain independence.

The Committee has noted that there are no contractual obligations to restrict the choice of external auditor. In accordance with best practice, the audit partner from the external auditor rotates off the audit engagement every 5 years.

The Audit Committee monitors non-audit services provided to the Group by the external auditor, recognising that there will be certain non-audit work which the external auditor is best placed to undertake.

The Committee's policy is to keep all services provided by the external auditor under review to ensure the independence and objectivity of the external auditor, taking account of relevant professional and regulatory requirements. Non-audit work over a certain value to be undertaken by the external auditor has to be approved by the Audit Committee in advance of any work being undertaken. Details of amounts paid to Deloitte LLP during 2019 for audit and other services are set out in note 2 to the financial statements.

### Audit tender process

In the context of its responsibility for the oversight of the effectiveness of the external audit process, the Audit Committee determined that it would put the external audit out to tender during the first half of 2019. Having assured itself of the independence of all Selection Panel members, the Board approved a Selection Panel ('the Panel') comprising the Chair of Audit Committee, the Group Finance Director and the Group Company Secretary to manage the tender process and to present a concluding recommendation to the Audit Committee and Board.

Ahead of the issuing of the invitation to tender letter, approaches were made to a number of firms, including firms other than the Big Four UK Audit practices, to advise them of the upcoming tender process and to invite them to confirm their interest in participating. In doing so, the Panel noted that the audit market choices available had to be assessed based on those firms who confirmed that they were able to offer the relevant expertise and experience to undertake the audit of a fully-listed company to an appropriate level of quality. The Panel concluded that it had undertaken all appropriate actions to secure the participation of all relevant audit firms, including non-Big Four auditors, to support an appropriately open but also robust and rigorous tender process.

In planning for the audit tender, the Panel considered any factors relevant to the independence of the participating firms. It was agreed that any potential conflicts in respect of work already in progress with the selected firms would be terminated in the event that one of these firms was successful.

The tender process was set out in the letter inviting firms to participate in the audit tender. The participating firms were given access to Group sites and personnel to enable them to attain the necessary knowledge of the Group's operations and finances to support their audit proposal. Each participating firm submitted a proposal document in advance of a presentation and Question and Answer session with the Panel. Documents received from the participating firms were reviewed and evaluated, with any concerns or areas for clarification being discussed with the firms during the presentations.

A standard scorecard and feedback form was completed by all key members of the Macfarlane team who met with the firms during their site visits as well as by members of the Panel following their review of each firm's proposal documents and presentation. These were reviewed by the entire Selection Panel as part of their evaluation of the firms.

The key evaluation criteria agreed by the Panel for the participating firms included:

- (i) Capability and competence to deliver a suitably robust and rigorous external audit;
- (ii) Quality and experience of the audit team, in particular the listed company experience of the lead audit partner;
- (iii) Developing knowledge of our business and applying it to the key judgements and risk areas;
- (iv) Effective communication skills with management and the Audit Committee on all aspects of the audit, financial reporting, internal control, corporate governance and risk management; and
- (v) Proactive development of data-driven procedures to improve the effectiveness and quality of the audit.

Whilst the level of fees proposed was not a significant consideration, participating firms were asked to confirm the arrangements under which fees would be reviewed for future years if there was no significant change in audit scope.

Based on the key evaluation criteria and ratings, and having considered all of the documents and other information available as a result of the tender process as described above, the Panel concluded that it should recommend to the Audit Committee and to the Board that Deloitte LLP be appointed as external auditor of Macfarlane Group with effect from 2019.

### **Risk management and internal control**

The Board is responsible for the Group's system of internal control and for reviewing its effectiveness. It is management's role to implement the Board's policies on risk and control through the design and operation of appropriate internal control systems. Such systems are designed to manage rather than eliminate the risk of failure to achieve business objectives and by their nature can only provide reasonable and not absolute assurance against material mis-statement or loss.

The Board confirms that an ongoing process for identifying, evaluating and managing the significant risks faced by the Group was in place in accordance with the principles of the Code and the related guidance. The process was in place throughout 2019 and has continued to the date of approval of the Annual Report and financial statements.

The Board regularly reviews the Group's system of internal control. The Board's monitoring covers all controls including financial, operational and compliance controls and risk management.

The key elements of the internal control process are:

- Formal Board reporting on a monthly basis by the Chief Executive and the Finance Director;
- Formal Board approval of the annual budget;
- Since 2009, Internal Audit has been staffed in-house. Certain parts of the internal audit plan may be outsourced when specific expertise is required. The Committee challenges and agrees the annual internal audit plan, receives reports on internal audit issues raised and a six-monthly update from the Head of Internal Audit;

- Monthly and annual financial control checklists submitted by each business unit;
- Discussion by the Committee of the external auditor's conclusions of its annual audit; and
- A robust risk assessment process as set out below.

Each business's risk register is kept under review during regular review meetings in each business. The Board considers the risk register every six months to maintain an overview of risks facing the Group and ensures that management has identified and implemented appropriate controls, which are acceptable to the Board, to address these risks. The risk register is taken into account in setting the internal audit plan each year.

The Audit Committee has received reports on cyber security matters to emphasise the importance of having robust cyber security measures in place as part of the controls framework, but also to ensure that employees, customers and suppliers are protected from the impact of cyber security breaches.

During the course of its review of the system of internal control, the Board has not identified nor been advised of any failings or weaknesses which it has determined to be significant. No significant corrective actions are outstanding.

The Directors have continued to review the effectiveness of the Group's system of financial and non-financial controls.

## Statement of Directors' responsibilities in respect of the Annual Report and the financial statements

### The Directors are responsible for preparing the Annual Report and 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 the Group financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and Article 4 of the IAS Regulation and have also chosen to prepare the parent Company financial statements in accordance with Financial Reporting Standard 101 'Reduced Disclosure Framework'.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent Company and of their profit or loss for that period.

In preparing the parent Company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether Financial Reporting Standard 101 'Reduced Disclosure Framework' has been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the Company will continue in business.

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

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

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

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

### Responsibility statement of the Directors in respect of the annual financial report

We confirm that to the best of our knowledge:

- The financial statements, prepared in accordance with the relevant financial reporting framework, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole;
- The Strategic Report, incorporated into the Directors' Report, includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face; and
- The Annual Report and 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 on 27 February 2020 and signed on its behalf by:



**Peter D. Atkinson**  
Chief Executive

27 February 2020



**John Love**  
Finance Director

27 February 2020



# Independent auditor's report to the members of Macfarlane Group PLC

## Report on the audit of the financial statements

### 1. Opinion

In our opinion:

- the financial statements of Macfarlane Group plc (the 'parent company') and its subsidiaries (the 'Group') give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2019 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, including Financial Reporting Standard 101 'Reduced Disclosure Framework'; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements which comprise:

- the consolidated income statement;
- the consolidated statement of comprehensive income;
- the consolidated and parent company balance sheets;
- the consolidated and parent company statements of changes in equity;
- the consolidated cash flow statement; and
- the related notes 1 to 42.

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

### 2. Basis for opinion

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

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

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

### 3. Summary of our audit approach

<b>Key audit matters</b>	<p>The key audit matters that we identified in our first year of appointment were:</p> <ul style="list-style-type: none"> <li>• Valuation of trade receivables, pinpointed to balances greater than 60 days and the completeness of the expected credit loss model.</li> <li>• Inflation, discount rate, and mortality assumptions used in calculating the defined benefit pension scheme liability.</li> </ul>
<b>Materiality</b>	<p>The materiality that we used for the Group financial statements was £600k which was determined on the basis of 5% of profit before tax.</p>
<b>Scoping</b>	<p>Our audit covered 98% of the Group's revenue, 96% of the Group's net assets, and 93% of the Group's profit before tax.</p>

## Independent auditor's report to the members of Macfarlane Group PLC (continued)

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

#### 4.1. Going concern

We have reviewed the Directors' statement within the accounting policies note to the financial statements about whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and their identification of any material uncertainties to the Group's and Company's ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements.

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

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

**Going concern is the basis of preparation of the financial statements that assumes an entity will remain in operation for a period of at least 12 months from the date of approval of the financial statements.**

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

#### 4.2. Principal risks and viability statement

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

- the disclosures on pages 18 and 19 that describe the principal risks, procedures to identify emerging risks, and an explanation of how these are being managed or mitigated;
- the Directors' confirmation on page 22 that they have carried out a detailed assessment of the principal and emerging risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity; or
- the Directors' explanation on page 22 as to how they have assessed the prospects of the Group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

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

**Viability means the ability of the Group to continue over the time horizon considered appropriate by the Directors.**

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

### 5. Key audit matters

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

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

### 5.1. Valuation of trade receivables, pinpointed to balances greater than 60 days and the completeness of the expected credit loss model

Key audit matter description	<p><b>The Group has material trade receivables, £46,695k (2018: £46,235k). A number of these receivables are individually material to the financial statements.</b></p> <p>The Group has a large number of customers and a significant trade receivables balance with the majority of sales on 60-75 day credit terms. Given the total value of trade receivables, we have identified a key audit matter around the risk that balances aged greater than 60 days (£1,339k) are not recoverable and in the completeness of the expected credit loss model.</p> <p>Due to the estimation uncertainty in the assessment of recoverability of receivables and in the calculation of the expected credit loss, we have determined that there is a potential for fraud through possible manipulation of the balance.</p> <p>Trade receivables are included within note 15. The Audit Committee's consideration in respect of the risk is included on page 49.</p>
How the scope of our audit responded to the key audit matter	<p>The audit procedures we performed in respect of this matter included:</p> <ul style="list-style-type: none"> <li>• Obtaining an understanding of the relevant controls relevant to the expected credit loss model;</li> <li>• Assessing the appropriateness of the assumptions, judgements and underlying data used in the expected credit loss model;</li> <li>• Challenging the recoverability of any debtors overdue for 90 days or longer;</li> <li>• Performing an analytical review of the year-end receivables balance using industry knowledge to challenge the recoverability of any receivables due from customers that we may consider to be in financial distress;</li> <li>• Selecting a significant risk sample of trade receivables aged greater than 60 days and a higher risk sample of all other trade receivables and agreeing to supporting documentation and, where possible, receipt of cash at bank post year-end; and</li> <li>• Analysing historical trends in raising credit notes, specifically looking at the volume and value raised throughout the year, not just after year-end.</li> </ul>
Key observations	<p>We concluded that the valuation of trade receivables recorded in the financial statements is not materially misstated. No misstatements were identified which warranted reporting to the Audit Committee.</p>

### 5.2. Inflation, discount rate and mortality assumptions used in calculating the defined benefit pension scheme liability

Key audit matter description	<p><b>Defined benefit obligation deficit recognised in the statement of financial position £6,465k (2018: £9,765k)</b></p> <p>The Group provides post-retirement benefits, including defined benefit pensions to employees. The Group engages a third party specialist, Aon Hewitt, to assist in the valuation of the defined benefit pension scheme liability. The valuation of gross liabilities as disclosed in note 25, is materially sensitive to small movements in key actuarial assumptions.</p> <p>There is a risk relating to the significant judgements made, specifically the discount rate, inflation and mortality assumptions used to derive the scheme liability.</p> <p>The Group's accounting policy notes that the actuarial assumptions are included as an area of key estimate uncertainty. Additional disclosures on the assumptions are included within note 25 of the financial statements, which includes details of the principal assumptions used as well as key movements in the assets and obligations of the scheme.</p>
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## Independent auditor's report to the members of Macfarlane Group PLC (continued)

### 5.2. Inflation, discount rate and mortality assumptions used in calculating the defined benefit pension scheme liability (continued)

<b>How the scope of our audit responded to the key audit matter</b>	<p>The audit procedures we performed in respect of this matter included:</p> <ul style="list-style-type: none"> <li>• Obtaining an understanding of the relevant controls relevant to the review of the assumptions used by the actuary.</li> <li>• Held a planning meeting with management, Aon Hewitt and our actuarial specialists to challenge the key assumptions.</li> <li>• Obtained internal controls reports for Aon and assessed their competency as scheme actuary.</li> <li>• Tested the estimates determined by management and their external actuary by challenging the appropriateness of the key assumptions used in the valuation of the scheme's liabilities. This was achieved by assessing these against benchmarked rates and through involvement of our actuarial specialists to review key assumptions.</li> <li>• Compared assumptions used to the Group's historical experience and market practice.</li> </ul>
<b>Key observations</b>	We consider each of the key assumptions both individually and in aggregate to be reasonable, and are in the middle of our acceptable ranges.

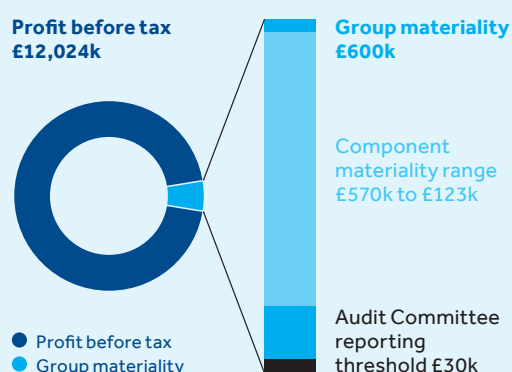
## 6. Our application of materiality

### 6.1. Materiality

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

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

	Group financial statements	Parent company financial statements
<b>Materiality</b>	£600k	£205k
<b>Basis for determining materiality</b>	5% of profit before tax	0.5% of net assets
<b>Rationale for the benchmark applied</b>	We have used profit before tax as the benchmark for our determination of materiality as we consider this to be the key performance metric for the Group and one which is a key metric to analysts and investors given the prominence in the Annual Report.	The main activity of the parent company is that of a holding company. The parent company holds the investments in the Group subsidiaries, the value of which is the key metric for the users of the financial statements.





## 6.2. Performance materiality

We set performance materiality at a level lower than materiality to reduce the probability that, in aggregate, uncorrected and undetected misstatements exceed the materiality for the financial statements as a whole. Group performance materiality was set at 70% of Group materiality for the 2019 audit. In determining performance materiality, we considered the following factors:

- This is our first year of engagement, however from our understanding gained in our acceptance and planning work, no issues have been identified within the control environment that have affected our ability to rely on controls and no significant control deficiencies have been identified.
- Our risk assessment did not identify a disproportionate number of significant risks of material misstatement.

## 6.3. Error reporting threshold

We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £30k, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We also report to the Audit Committee on disclosure matters that we identified when assessing the overall presentation of the financial statements.

## 7. An overview of the scope of our audit

### 7.1. Identification and scoping of components

Our Group audit was scoped by obtaining an understanding of the Group and its environment through discussion with IT, internal audit, and the Group and component finance teams and by performing walkthroughs of processes across each of these areas, including Group-wide controls, and assessing the risk of material misstatement at a Group level.

For components deemed significant to the Group, full scope audit procedures were performed to materiality levels applicable to each entity, which was lower than the Group materiality level. Components deemed significant are as follows:

- Macfarlane Group UK Limited
- Nelsons for Cartons & Packaging Limited
- Macfarlane Labels Limited
- Macfarlane Group Ireland (Labels & Packaging) Limited

Macfarlane Labels generates revenues in both Europe and the UK while other Group entities operate primarily within the UK where 97% of total revenues are generated. Each legal entity operating in the UK generates revenue through a range of services and customer bases.

This provided audit coverage of over 98% of the Group's revenue, 96% of the Group's net assets and 93% of the Group's profit.

The remaining non-significant components were subject to analytical reviews. Our audit work on these components was executed at Group materiality.

At the parent entity level, we also tested the consolidation process.

All work on the significant components and consolidation process was performed by the Group engagement team.

## Independent auditor's report to the members of Macfarlane Group PLC (continued)

### 8. Other information

The Directors are responsible for the other information. The other information comprises the information included in the annual report (including the Chairman's statement, Macfarlane Group Business Model and Strategy, Chief Executive's review, Report of the Directors, Remuneration Report, Corporate Governance Report and Statement of Directors' Responsibilities), other than the financial statements and our auditor's report thereon.

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

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

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

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

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

We have nothing to report in respect of these matters.

### 9. Responsibilities of Directors

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

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

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

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

Details of the extent to which the audit was considered capable of detecting irregularities, including fraud and non-compliance with laws and regulations are set out below.

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

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

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

### 11.1 Identifying and assessing potential risks related to irregularities

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

- the nature of the industry and sector, control environment and business performance including the design of the Group's remuneration policies, key drivers for Directors' remuneration, bonus levels and performance targets;
- results of our enquiries of management, internal audit and the audit committee about their own identification and assessment of the risks of irregularities;
- any matters we identified having obtained and reviewed the Group's documentation of their policies and procedures relating to:
  - identifying, evaluating and complying with laws and regulations and whether they were aware of any instances of non-compliance;
  - detecting and responding to the risks of fraud and whether they have knowledge of any actual, suspected or alleged fraud;
  - the internal controls established to mitigate risks of fraud or non-compliance with laws and regulations;
- the matters discussed among the audit engagement team and involving relevant internal specialists, including valuations, pensions, and IT specialists regarding how and where fraud might occur in the financial statements and any potential indicators of fraud.

As a result of these procedures, we considered the opportunities and incentives that may exist within the organisation for fraud and identified the greatest potential for fraud in relation to the valuation of trade receivables and given the assumptions and judgements included in preparing the expected credit loss model. In common with all audits under ISAs (UK), we are also required to perform specific procedures to respond to the risk of management override.

We also obtained an understanding of the legal and regulatory frameworks that the Group operates in, focusing on provisions of those laws and regulations that had a direct effect on the determination of material amounts and disclosures in the financial statements. The key laws and regulations we considered in this context included The Companies Act 2006, The UK Corporate Governance Code, The Listing Rules, and Tax Law.

In addition, we considered provisions of other laws and regulations that do not have a direct effect on the financial statements but compliance with which may be fundamental to the Group's ability to operate or to avoid a material penalty. These include UK Employment and Labour Laws and UK Packaging Regulations.

### 11.2 Audit response to risks identified

As a result of performing the above, we identified valuation of trade receivables as a key audit matter related to the potential risk of fraud. The key audit matters section of our report explains the matter in more detail and also describes the specific procedures we performed in response to that key audit matter.

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

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

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

## Independent auditor's report to the members of Macfarlane Group PLC (continued)

### Report on other legal and regulatory requirements

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

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

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

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

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

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

##### 13.1 Adequacy of explanations received and accounting records

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

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

We have nothing to report in respect of these matters.

##### 13.2 Directors' remuneration

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

We have nothing to report in respect of these matters.

#### 14. Other matters

##### 14.1 Auditor tenure

Following the recommendation of the audit committee, we were appointed by the Board of Directors on 12 July 2019 to audit the financial statements for the year ending 31 December 2019 and subsequent financial periods. The period of total uninterrupted engagement including previous renewals and reappointments of the firm is 1 year, covering the year ending 31 December 2019.

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

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

#### 15. Use of our report

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



**David Sweeney CA (Senior Statutory Auditor)**

For and on behalf of Deloitte LLP

Statutory Auditor

Glasgow, United Kingdom

27 February 2020



## Consolidated income statement

For the year ended 31 December 2019

	Note	2019 £000	2018 Before exceptional item £000	Exceptional item* £000	2018 £000
<b>Continuing operations</b>					
Revenue	1	<b>225,389</b>	217,290	–	217,290
Cost of sales		<b>(153,256)</b>	(150,749)	–	(150,749)
<b>Gross profit</b>		<b>72,133</b>	66,541	–	66,541
Distribution costs		<b>(8,441)</b>	(8,604)	–	(8,604)
Administrative expenses		<b>(50,062)</b>	(45,912)	(330)	(46,242)
<b>Operating profit*</b>	1,2	<b>13,630</b>	12,025	(330)	11,695
Finance costs	5	<b>(1,606)</b>	(809)	–	(809)
<b>Profit before tax*</b>		<b>12,024</b>	11,216	(330)	10,886
Tax	6	<b>(2,293)</b>	(2,201)	56	(2,145)
<b>Profit for the year*</b>	21	<b>9,731</b>	9,015	(274)	8,741
<b>Earnings per share*</b>	9				
Basic		<b>6.17p</b>	5.72p	(0.17p)	5.55p
Diluted		<b>6.16p</b>	5.72p	(0.17p)	5.55p

\* Details of the 2018 exceptional item are set out in note 3.

## Consolidated statement of comprehensive income

For the year ended 31 December 2019

	Note	2019 £000	2018 £000
<b>Items that may be reclassified to profit or loss</b>			
Foreign currency translation differences	21	<b>(62)</b>	(6)
<b>Items that will not be reclassified to profit or loss</b>			
Remeasurement of pension scheme liability	25	<b>537</b>	(32)
<b>Tax recognised in other comprehensive income</b>			
Tax on remeasurement of pension scheme liability	19	<b>(92)</b>	6
<b>Other comprehensive income/(expense) for the year, net of tax</b>		<b>383</b>	(32)
Profit for the year		<b>9,731</b>	8,741
<b>Total comprehensive income for the year</b>		<b>10,114</b>	8,709

## Consolidated statement of changes in equity

For the year ended 31 December 2019

	Note	Share capital £000	Share premium £000	Revaluation reserve £000	Translation reserve £000	Retained earnings £000	Total £000
At 1 January 2018		39,387	12,975	70	299	4,479	57,210
<b>Comprehensive income</b>							
Profit for the year		–	–	–	–	8,741	8,741
Foreign currency translation differences	21	–	–	–	(6)	–	(6)
Remeasurement of pension scheme liability	25	–	–	–	–	(32)	(32)
Tax on remeasurement of pension scheme liability	19	–	–	–	–	6	6
<b>Total comprehensive income</b>		–	–	–	(6)	8,715	8,709
<b>Transactions with shareholders</b>							
Dividends	8	–	–	–	–	(3,387)	(3,387)
<b>Total transactions with shareholders</b>		–	–	–	–	(3,387)	(3,387)
At 31 December 2018		<b>39,387</b>	<b>12,975</b>	<b>70</b>	<b>293</b>	<b>9,807</b>	<b>62,532</b>
<b>Comprehensive income</b>							
Profit for the year		–	–	–	–	<b>9,731</b>	<b>9,731</b>
Foreign currency translation differences	21	–	–	–	<b>(62)</b>	–	<b>(62)</b>
Remeasurement of pension scheme liability	25	–	–	–	–	<b>537</b>	<b>537</b>
Tax on remeasurement of pension scheme liability	19	–	–	–	–	<b>(92)</b>	<b>(92)</b>
<b>Total comprehensive income</b>		–	–	–	<b>(62)</b>	<b>10,176</b>	<b>10,114</b>
<b>Transactions with shareholders</b>							
Dividends	8	–	–	–	–	<b>(3,689)</b>	<b>(3,689)</b>
Share-based payments	26	–	–	–	–	<b>75</b>	<b>75</b>
Issue of share capital	20,21	<b>66</b>	<b>173</b>	–	–	–	<b>239</b>
<b>Total transactions with shareholders</b>		<b>66</b>	<b>173</b>	–	–	<b>(3,614)</b>	<b>(3,375)</b>
At 31 December 2019		<b>39,453</b>	<b>13,148</b>	<b>70</b>	<b>231</b>	<b>16,369</b>	<b>69,271</b>

# Consolidated balance sheet

At 31 December 2019

	Note	2019 £000	2018 £000
<b>Non-current assets</b>			
Goodwill and other intangible assets	10	62,663	58,648
Property, plant and equipment	11	9,621	8,533
Right of use assets	12	25,855	–
Trade and other receivables	15	35	162
Deferred tax assets	19	1,224	1,851
<b>Total non-current assets</b>		<b>99,398</b>	69,194
<b>Current assets</b>			
Inventories	14	15,813	16,940
Trade and other receivables	15	52,044	51,360
Cash and cash equivalents	16	3,310	4,611
<b>Total current assets</b>		<b>71,167</b>	72,911
<b>Total assets</b>	1	<b>170,565</b>	142,105
<b>Current liabilities</b>			
Trade and other payables	17	48,530	47,891
Current tax liabilities		1,084	1,029
Lease liabilities	18	6,321	101
Bank borrowings	16	15,984	17,769
<b>Total current liabilities</b>		<b>71,919</b>	66,790
<b>Net current (liabilities)/assets</b>		<b>(752)</b>	6,121
<b>Non-current liabilities</b>			
Retirement benefit obligations	25	6,465	9,765
Deferred tax liabilities	19	3,242	2,993
Trade and other payables	17	22	25
Lease liabilities	18	19,646	–
<b>Total non-current liabilities</b>		<b>29,375</b>	12,783
<b>Total liabilities</b>	1	<b>101,294</b>	79,573
<b>Net assets</b>	1	<b>69,271</b>	62,532
<b>Equity</b>			
Share capital	20	39,453	39,387
Share premium	21	13,148	12,975
Revaluation reserve	21	70	70
Translation reserve	21	231	293
Retained earnings	21	16,369	9,807
<b>Total equity</b>		<b>69,271</b>	62,532

The financial statements of Macfarlane Group PLC, Company registration number SC004221, were approved by the Board of Directors on 27 February 2020 and signed on its behalf by



**Peter D. Atkinson**  
Chief Executive



**John Love**  
Finance Director

Overview

Strategic review

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## Consolidated cash flow statement

For the year ended 31 December 2019

	Note	2019 £000	2018 £000
<b>Net cash inflow from operating activities</b>	23	<b>19,497</b>	11,832
<b>Investing activities</b>			
Acquisitions	24	<b>(6,162)</b>	(5,638)
Proceeds from disposal of property, plant and equipment		<b>185</b>	73
Purchase of property, plant and equipment		<b>(2,648)</b>	(1,452)
<b>Cash outflow from investing activities</b>		<b>(8,625)</b>	(7,017)
<b>Financing activities</b>			
Dividends paid	8	<b>(3,689)</b>	(3,387)
(Repayment)/drawdown of bank borrowing facility	23	<b>(1,785)</b>	1,423
Repayment of lease obligations	23	<b>(6,699)</b>	(253)
<b>Cash outflow from financing activities</b>		<b>(12,173)</b>	(2,217)
<b>Net (decrease)/increase in cash and cash equivalents</b>		<b>(1,301)</b>	2,598
Cash and cash equivalents at beginning of year		<b>4,611</b>	2,013
<b>Cash and cash equivalents at end of year</b>	23	<b>3,310</b>	4,611

There is no material impact of foreign exchange rate differences on the cash and cash equivalents balance at the end of the current or preceding financial year.



# Accounting policies

For the year ended 31 December 2019

## Basis of preparation

Macfarlane Group PLC is a public company listed on the London Stock Exchange, incorporated and domiciled in the United Kingdom and registered in Scotland. The Company's registered office is 3 Park Gardens, Glasgow, G3 7YE.

## Basis of accounting

The principal activities of the Company and its subsidiaries (the Group) and the nature of the Group's operations are set out in the strategic report on pages 4 to 29. The 2019 financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and therefore the Group financial statements comply with Article 4 of the EU IAS Regulation. These consolidated financial statements are presented in Sterling, which is the Company's functional currency. All amounts have been rounded to the nearest thousand, unless otherwise indicated.

The financial statements have been prepared on the historical cost basis. The revaluation reserve relates to a period before transition to IFRS.

In measuring the financial performance and position, the financial measures used include those which have been derived from the reported results in order to eliminate factors which distort year-on-year comparisons and/or provide useful information to stakeholders. These are considered non-GAAP financial measures and include measures such as operating profit before exceptional items and profit before tax and exceptional items. We believe this information along with comparable GAAP measurements is useful in providing a basis for measuring the financial performance and position. Note 3 includes further information on these non-GAAP financial measures which were applied in 2018. There were no items classified as exceptional in the 2019 results.

## Going concern

The Directors, in their consideration of going concern, have reviewed the Group's future cash flow forecasts and profit projections, which they believe are based on an appropriate assessment of the market and past experience. The Group's business activities, together with the factors likely to affect its future development, performance and financial position are set out in the Strategic Report on pages 4 to 29.

The Group's principal financial risks in the medium term relate to liquidity and credit risk. Liquidity risk is managed by ensuring that the Group's day-to-day working capital requirements are met by having access to banking facilities with suitable terms and conditions to accommodate the requirements of the Group's operations. The Group has a committed borrowing facility of £30 million with Lloyds Banking Group PLC in place until June 2022. The facility bears interest at normal commercial rates and carries standard financial covenants in relation to interest cover and levels of headroom over trade receivables. Credit risk is mitigated by applying considerable rigour in managing the Group's trade receivables. The Directors believe that the Group is adequately placed to manage its financial risks effectively, despite any economic uncertainty.

The Directors are of the opinion that the Group's cash flow forecasts and profit projections, which they believe are based on a prudent assessment of the market and past experience taking account of reasonably possible changes in trading performance given current market and economic conditions, show that the Group should be able to operate within the current facility and comply with its banking covenants.

After making enquiries, the Directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for a period extending at least the next twelve months from the date of approval of these financial statements. For this reason they continue to adopt the going concern basis in preparing the financial statements.

## Key sources of estimation uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported for assets and liabilities as at the balance sheet date and the amounts reported for revenues and expenses during the year. Due to the nature of estimation, the actual outcomes may well differ from these estimates. No significant judgements have been made in the current or prior year.

The key sources of estimation uncertainty that have a significant effect on the carrying amounts of assets and liabilities are discussed below:

## Retirement benefit obligations

The determination of any defined benefit pension scheme liability is based on assumptions determined with independent actuarial advice. The key assumptions used include discount rate, inflation rate and mortality assumptions, for which a sensitivity analysis is provided in note 25. The Directors consider that those sensitivities represent reasonable sensitivities which could occur in the next financial year.

## Accounting policies (continued)

For the year ended 31 December 2019

### Valuation of trade receivables

The provision held against trade receivables is based on applying an expected credit loss model and related estimates of recoverable amounts, as detailed in note 15. Whilst every attempt is made to ensure that the provision held against doubtful trade receivables is as accurate as possible, there remains a risk that the provision may not match the level of debt, which ultimately proves uncollectable. An increase in the average default rate of trade receivables beyond terms from 1.04% to 3.12% above the historic loss rates observed would lead to an increase in the provision recognised of £600,000.

### Changes in accounting policies in 2019

This is the first set of financial statements where IFRS 16 'Leases' has been applied, with an initial application date of 1 January 2019. IFRS 16 introduces significant changes to lessee accounting by removing the distinction between operating and finance leases, requiring the recognition of a right-of-use asset and a lease liability at commencement for all leases, except for short-term leases and leases of low value assets.

The Company has a large number of property and equipment leases. Details of the Company's accounting policies under IFRS 16 are set out below, followed by details of the impact on adoption of IFRS 16. Judgements applied in the adoption of IFRS 16 included determining the lease term for those leases with termination or extension options and determining an incremental borrowing rate where the rate implicit in a lease could not be readily determined.

Whilst there has been no significant impact on profit before tax or net assets from applying the new standard, there are changes in classifications from the adoption of IFRS 16 in 2019 indicated throughout these financial statements.

### New accounting standards and interpretations

The Group is currently assessing the potential impact of new and revised standards and interpretations issued by the IASB that will be effective from 1 January 2020. None of these have been adopted early.

IFRS 17	Insurance Contracts
IFRS 10 and IAS 28 (amendments)	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture
Amendments to IFRS 3	Definition of a business
Amendments to IAS 1 and IAS 8	Definition of material
Conceptual Framework	Amendments to References to the Conceptual Framework in IFRS Standards

The Directors do not expect that the adoption of the Standards listed above will have a material impact on the financial statements of the Group in future periods.

### Summary of accounting policies

The following accounting policies have been applied consistently for items which are considered to be material in relation to the financial statements.

#### (a) Basis of consolidation

The consolidated income statement and the consolidated balance sheet include the financial statements of the parent company and its subsidiaries, all of which are wholly-owned, to the end of the financial year. The Group does not have any associates or other joint arrangements as defined by IFRS 10 'Consolidated Financial Statements'.

#### Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group is exposed to, 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. In assessing control, the Group takes into consideration potential voting rights. The acquisition date is the date on which control is transferred to the acquirer.

The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

#### Business combinations

The acquisition of subsidiaries is accounted for under the acquisition method. The acquired business is measured at the effective date of acquisition, defined as the date control is acquired, as the aggregate fair value of assets, liabilities and contingent liabilities as required under IFRS 3 'Business Combinations'. Any excess of the cost of acquisition over the fair value of the separately identifiable net assets of the acquired business is represented as goodwill. Contingent consideration classified as a liability will be subsequently re-measured through the consolidated income statement.

The results of subsidiaries acquired or disposed of during the period are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal. The consolidated gain or loss on disposal of a subsidiary is the difference between the net proceeds of sale and the Group's share of the subsidiary's net assets together with the carrying value of any related goodwill at the effective date of disposal.

## Transactions eliminated on consolidation

Intra-Group balances and transactions, and any unrealised income and expenses arising from intra-Group transactions, are eliminated.

## (b) Goodwill and other intangible assets

### Goodwill

Goodwill arising on a business combination is recognised as an asset and represents the excess of the cost of acquisition over the net fair values of the separately identifiable assets and liabilities of the acquired business or subsidiary at the effective date of acquisition.

Goodwill is allocated to cash generating units ('CGUs') expected to benefit from the synergies of the combination, for the purpose of impairment testing. The carrying value of goodwill for each CGU is considered annually and also reviewed where management has reason to believe that a change in circumstances may give rise to any impairment or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

### Other intangible assets

Other intangible assets comprise separately identifiable intangible assets recognised on the acquisitions of businesses or subsidiary companies. They are recorded at fair value on acquisition less any amortisation and subsequent impairment. These are primarily Brand values, which are calculated on the Relief from Royalty method, and Customer relationship values, which are calculated on the Excess Earnings method based on the net anticipated earnings stream. Brand values are amortised on a straight-line basis over up to five years and Customer relationships are amortised on a straight-line basis over ten years.

### Impairment

The carrying values of the Group's assets are reviewed annually to determine if there is any indication of impairment. If any such indication exists, the assets' recoverable values are calculated as the present value of the estimated future cash flows, discounted at appropriate pre-tax discount rates. Impairment losses are recognised when the carrying value of an asset or CGU exceeds recoverable value. Impairment losses are recognised in the consolidated income statement.

## (c) Revenue recognition

The Group is engaged in the delivery of packaging materials, packing machinery, labels and labels machinery to customers. Revenue is not recognised if there is significant uncertainty regarding the recovery of the revenue consideration. Revenue represents amounts receivable for goods provided to third parties in the normal course of business, net of discounts, customer rebates, VAT and other sales related taxes.

IFRS 15 '*Revenue from Contracts with Customers*' requires the Group to apportion revenues from customer contracts to separate performance obligations and recognise revenues as each performance obligation is satisfied. The Group has reviewed its arrangements with customers and concluded that the Group's revenue is generated from the delivery of the goods to customers and that this represents a single performance obligation. The Group does not enter into any repurchase agreements. It is therefore appropriate to recognise revenue at the point of transfer of goods to the customer, consistent with the revenue recognition framework in IFRS 15.

## (d) Leasing

From 1 January 2019, the Company recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets below £4,000. For these short-term or low value leases, the Company recognises the lease payments as an operating expense disclosed in administrative expenses on a straight-line basis over the term of the lease.

For all other leases, the lease liability is initially measured at the present value of lease payments that are not paid at the commencement date, discounted using the rate implicit in the lease. If this rate cannot be readily determined, the Company uses its incremental borrowing rate.

Lease liabilities are presented on two separate lines in the balance sheet for creditors due within one year and creditors due outwith one year. The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method) and by reducing the liability by payments made. The Company remeasures the lease liability (and adjusts the related right-of-use asset) whenever the lease term has changed or a lease contract is modified and the modification is not accounted for as a separate lease. The Company did not make any such adjustments during the period presented.

Right-of-use ('ROU') assets comprise the initial measurement of the corresponding lease liability and are subsequently measured at cost less accumulated depreciation and impairment losses.

## Accounting policies (continued)

For the year ended 31 December 2019

### (d) Leasing (continued)

ROU assets are depreciated over the shorter period of lease term and useful life of the underlying asset. If a lease transfers ownership of the underlying asset or the cost of the ROU asset reflects that the Company expects to exercise a purchase option, the related ROU asset is depreciated over the useful life of the asset. Depreciation starts on the commencement date of the lease.

ROU assets are presented within the same category as that within which the corresponding underlying assets would be presented if they were owned – for the Company these two categories are property and plant, machinery, vehicles and fittings.

As a practical expedient, IFRS 16 permits a lessee not to separate non-lease components, and instead account for any lease and associated non-lease components as a single arrangement. The Company has not used this practical expedient and has separated out the non-lease components for its leases. These non-lease components, typically servicing and maintenance costs, have been recognised as an expense on a straight-line basis and disclosed in administrative expenses in the consolidated income statement.

### Approach to transition

The Company has applied IFRS 16 using the modified retrospective approach, without restatement of the comparative information. For leases previously treated as operating leases, the Company has elected to follow the approach in IFRS 16, C8(b)(ii), whereby right of use assets are set equal to the lease liability, adjusted for prepaid or accrued lease payments, including unamortised lease incentives.

The Group's incremental borrowing rates applied to lease liabilities as at 1 January 2019 range between 2.75% and 4.00%.

### Practical expedients adopted on transition

As part of the Company's adoption of IFRS 16 and application of the modified retrospective approach to transition, the Company elected to use the following practical expedients:

- a single discount rate has been applied to assets with reasonably similar characteristics; and
- hindsight has been used in determining the lease term.

### Impact on disclosures

#### Former operating leases

IFRS 16 changes accounting for leases previously classified as operating leases under IAS 17, which were off-balance sheet. Applying IFRS 16, for all leases, the Company now recognises ROU assets and lease liabilities on the balance sheet, initially measured as described above. Lease incentives are recognised as part of the measurement of the ROU assets and lease liabilities, whereas under IAS 17 they resulted in the recognition of a lease incentive liability, amortised as a reduction of rental expenses on a straight line basis.

ROU assets will be tested for impairment in accordance with IAS 36 Impairment of Assets.

Under IFRS 16 the Company recognises depreciation of ROU assets and interest on lease liabilities in the consolidated income statement, whereas operating leases previously gave rise to leasing costs in administrative expenses.

#### Former finance leases

This change has not had a material effect in the financial statements.

### Financial impact of IFRS 16 'Leases'

The table below sets out adjustments recognised at 1 January 2019, the date of initial application.

	As previously reported 31 December 2018 £000	Impact of IFRS 16 £000	At 1 January 2019 £000
<b>Assets</b>			
Right of Use assets	–	<b>27,476</b>	27,476
Debtors	51,522	<b>487</b>	52,009
<b>Impact on total assets</b>		<b>27,963</b>	
<b>Liabilities</b>			
Lease liabilities	(101)	<b>(27,963)</b>	(28,064)
<b>Impact on total liabilities</b>		<b>(27,963)</b>	
<b>Net assets/shareholder's funds</b>	62,532	<b>–</b>	62,532



The table below presents a reconciliation from operating lease commitments disclosed at 31 December 2018 to the finance lease assets and liabilities recognised at 1 January 2019.

	Receivable €000	Payable €000
Operating lease commitments at 31 December 2018 under IAS 17	738	(35,575)
Non-lease components expensed under IFRS 16	—	2,805
Short-term and low value leases	—	942
Effect of discounting	(26)	3,865
Finance lease assets/(liabilities) recognised at 31 December 2018	—	(101)
Total finance lease assets/(liabilities) recognised at 1 January 2019	712	(28,064)

Movements in lease liabilities in 2019 are set out in note 23.

The application of IFRS 16 resulted in a decrease in other operating expenses and an increase in depreciation and interest expense compared to IAS 17. During 2019, for all leases the Group recognised the following amounts in the consolidated income statement.

	2019 €000
Depreciation	6,223
Interest expense	810
Operating lease payments made in 2019	6,806
Decrease in profit from applying IFRS 16 in 2019	227

### (e) Foreign currencies

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are retranslated to the functional currency at the exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the consolidated income statement. Non-monetary assets and liabilities, measured at historical cost in a foreign currency, are translated using the exchange rates at the date of the transaction. Non-monetary assets and liabilities, stated at fair value in a foreign currency, are retranslated to the functional currency at the exchange rates ruling at the dates the fair value was determined.

Assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to the Group's presentational currency, Sterling, at the exchange rates ruling at the balance sheet date. Revenues and expenses of foreign operations are translated at an average rate for the year where this rate approximates to the exchange rates ruling at the dates of the transactions. Exchange differences arising from the translation of foreign operations are reported as an item of other comprehensive income and accumulated in the translation reserve.

### (f) Retirement benefits

#### Defined contribution schemes

A defined contribution scheme is a post-employment benefit scheme under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension schemes are recognised as an expense in the consolidated income statement in the periods during which services are rendered by employees.

#### Defined benefit schemes

A defined benefit scheme is a post-employment benefit scheme other than a defined contribution scheme. The Group's net retirement benefit obligation in respect of its defined benefit pension scheme is calculated by estimating the amount of future benefits that employees have earned in return for their service in current and prior periods. These benefits are then discounted to determine the present value, and the fair values of any scheme investments, at bid price, are deducted. The net interest on the net retirement benefit obligation for the year is calculated by applying the discount rate used to measure the defined benefit obligation at the beginning of the year.

The discount rate is the yield at the reporting date on bonds that have a credit rating of at least AA that have maturity dates approximating to the average duration of the Group's retirement benefit obligations and that are denominated in the currency in which the benefits are expected to be paid.

## Accounting policies (continued)

For the year ended 31 December 2019

### (f) Retirement benefits (continued)

Remeasurements arising from defined benefit plans comprise actuarial gains and losses, returns on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest). Remeasurements are recognised in the statement of other comprehensive income and all other expenses related to defined benefit schemes charged in staff costs in the consolidated income statement.

When the benefits of a scheme are changed, or when a scheme is curtailed, the portion of the changed benefit related to past service by employees, or the gain or loss on curtailment, is recognised immediately in the consolidated income statement when the scheme amendment or curtailment occurs.

The calculation of the retirement benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of the present value of any minimum funding requirements.

The Group's defined benefit pension scheme covers the Group companies at December 2002. The net defined benefit cost of the scheme is apportioned to these participating entities based on the employment history of scheme members, who are allocated to the relevant subsidiary, with any remaining members allocated to the parent company.

### (g) Taxation

The tax expense represents the sum of the current tax payable and deferred tax.

Current tax is payable based on the taxable profit for the year. Taxable profit differs from profit before tax as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and excludes items that are never taxable or deductible. The current tax liability is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date and any adjustments in respect of prior years.

Deferred tax balances represent the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax assets and liabilities are not discounted.

The carrying value of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities are generally recognised for all taxable temporary differences.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised based on tax laws and rates that have been substantively enacted at the balance sheet date. Deferred tax is charged or credited in the consolidated income statement, except when it relates to items charged or credited in other comprehensive income, in which case the deferred tax is also recorded in the consolidated statement of other comprehensive income.

### (h) Property, plant and equipment

Property, plant and equipment are stated at cost, with assets revalued before the date of transition to IFRS recorded at deemed cost.

No depreciation is provided on land. Depreciation is recognised so as to write off the cost of the property, plant and equipment, less their estimated residual values, by equal annual instalments over their estimated useful lives. The rates of depreciation use the straight-line method and vary between 2% and 5% per annum on buildings and 7% and 33% per annum on plant and equipment. Rates of depreciation are reviewed annually to ensure they remain relevant and residual values are reviewed to ensure they remain appropriate once in each calendar year.

### (i) Inventories

Inventories are consistently stated at the lower of cost and net realisable value. Cost represents purchase price. In the case of work in progress and finished goods, cost comprises direct materials, direct labour costs and attributable overheads that have been incurred in bringing the inventories to their present location and condition. Net realisable value is based on the estimated selling price, less any further costs expected to be incurred to completion and disposal. Inventories are stated less provisions required for slow-moving and obsolete items, where appropriate.

## (j) Financial instruments

Financial assets and financial liabilities are recognised in the Group's balance sheet when the Group becomes a party to the contractual provisions of the instrument.

**Financial assets** categorised as investments, comprise investments in debt and equity securities and are initially recognised at fair value with any subsequent gains or losses recognised in the consolidated income statement.

Other financial assets comprise trade and other receivables that have fixed or determinable recoveries. The classification takes account of the nature and purpose of the financial assets and is determined on initial recognition. Trade and other receivables are measured at amortised cost less impairment under the expected credit loss model.

Indicators are assessed for the impairment of financial assets at each balance sheet date. Financial assets are impaired when there is objective evidence that as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows have been impacted. For trade receivables the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is measured on an expected credit loss model at inception rather than an incurred loss model. When a trade receivable is uncollectible, it is written off against the provision made on inception or at a previous reporting period end. Subsequent recoveries of amounts previously written off are credited against the provision. In accordance with IFRS 9 'Financial Instruments' changes in the carrying value of the provision are recognised in the consolidated income statement.

**Cash and cash equivalents** comprise cash on hand and on demand deposits, readily convertible to a known amount of cash and are subject to insignificant risk of changes in value.

**Financial liabilities and equity instruments** are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements.

Financial liabilities comprise solely other financial liabilities under the terms of IFRS 7. Financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortised cost, with interest expense measured on an effective yield basis.

Equity instruments are any contracts evidencing a residual interest in the assets of the Company after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Derivative financial instruments were not used in the current or preceding financial year.

## (k) Exceptional items

Where items arise that would distort the presentation of the results for the year, the Directors will classify such items as exceptional in nature and provide details of the items to enable users of the accounts to understand the impact on the financial statements.

## (l) Provisions

The Group has a small number of surplus properties, where it seeks to obtain rental income from a sub-lease to cover its ongoing liabilities under the head lease. In the event that a property held under one of these leases becomes vacant due to the expiry of a sub-lease, every effort is made to attract a new tenant. If there is likely to be a rental void for a period of time, then a provision is made at each balance sheet date to cover management's best estimate of the future cost of the likely void period.

## (m) Share-based payments

The grant date fair value of share-based payments awards granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the awards. The fair value of the awards granted is measured using an option valuation model, taking into account the terms and conditions upon which the awards were granted. The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date. For share-based payment awards with non-vesting conditions, the grant date fair value of the share-based payment is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

Details of the determination of the fair value of equity-settled share-based transactions are set out in note 26.

# Notes to the financial statements

For the year ended 31 December 2019

## 1. Business and geographical segments

### (a) Business segments

The Group's principal business segment is Packaging Distribution, comprising the distribution of packaging materials and supply of storage and warehousing services in the UK. This comprises over 85% of Group revenue and profit. The Group's Manufacturing Operations segment comprises the design, manufacture and assembly of timber, corrugated and foam-based packaging materials in the UK, the design, manufacture and supply of self-adhesive labels to a variety of FMCG customers in the UK & Europe and the design, manufacture and supply of resealable labels to a variety of FMCG customers in the UK, Europe and the USA. None of the business segments within Manufacturing Operations represents more than 10% of Group revenue or profit.

External revenues from major products and services	2019 £000	2018 £000
Packaging Distribution	196,706	189,835
Design, manufacture and assembly of timber, corrugated and foam-based packaging materials	10,642	10,709
Manufacture and supply of self-adhesive labels	9,148	8,337
Manufacture and supply of resealable labels and related machinery	8,893	8,409
<b>External revenues from Continuing operations</b>	<b>225,389</b>	217,290

### (b) Segmental information

	Packaging Distribution £000	Manufacturing Operations £000	2019 Total £000	Packaging Distribution £000	Manufacturing Operations £000	2018 Total £000
<b>Revenue</b>						
Total revenue	196,706	34,016	230,722	190,227	32,189	222,416
Inter-segment revenue	–	(5,333)	(5,333)	(392)	(4,734)	(5,126)
External revenue	196,706	28,683	225,389	189,835	27,455	217,290
Cost of sales	(135,525)	(17,731)	(153,256)	(133,843)	(16,906)	(150,749)
<b>Gross profit</b>	<b>61,181</b>	<b>10,952</b>	<b>72,133</b>	55,992	10,549	66,541
Net operating expenses	(48,775)	(9,728)	(58,503)	(44,820)	(9,696)	(54,516)
<b>Operating profit before exceptional item</b>	<b>12,406</b>	<b>1,224</b>	<b>13,630</b>	11,172	853	12,025
Exceptional item	–	–	–	(270)	(60)	(330)
<b>Operating profit</b>	<b>12,406</b>	<b>1,224</b>	<b>13,630</b>	10,902	793	11,695
Net finance costs			(1,606)			(809)
<b>Profit before tax</b>			<b>12,024</b>			10,886
Tax			(2,293)			(2,145)
<b>Profit for the year</b>			<b>9,731</b>			8,741

Inter-segment revenues are charged at prevailing market prices.

	Packaging Distribution £000	Manufacturing Operations £000	2019 Total £000	Packaging Distribution £000	Manufacturing Operations £000	2018 Total £000
Capital additions	12,074	1,805	13,879	4,722	473	5,195
Depreciation/amortisation	9,179	1,033	10,212	3,350	487	3,837
Segment assets	151,115	19,450	170,565	125,060	17,045	142,105
Segment liabilities	(90,508)	(10,786)	(101,294)	(71,173)	(8,400)	(79,573)
<b>Net assets</b>	<b>60,607</b>	<b>8,664</b>	<b>69,271</b>	53,887	8,645	62,532

### (c) Geographical segments

The Group's operations are primarily located in the UK and Europe.

Packaging Distribution activities are primarily in the UK.

Within Manufacturing Operations, the Packaging Design and Manufacture business operates primarily in the UK and the Labels businesses operate in the UK, Europe and through distributors in the USA.

	Continuing operations UK €000	Europe €000	2019 Total €000	Continuing operations UK €000	Europe €000	2018 Total €000
<b>External revenue</b>	<b>219,310</b>	<b>6,079</b>	<b>225,389</b>	211,975	5,315	217,290
<b>Operating profit</b>	<b>13,170</b>	<b>460</b>	<b>13,630</b>	11,310	385	11,695
<b>Non-current assets</b>	<b>89,719</b>	<b>9,679</b>	<b>99,398</b>	67,444	1,750	69,194
<b>Capital additions</b>	<b>12,994</b>	<b>885</b>	<b>13,879</b>	5,141	54	5,195

### (d) Information about major customers

No single customer accounts for more than 5% of the Group's external revenues and customer dependencies are regularly monitored.

## 2. Operating profit

<b>Operating profit has been arrived at after charging:</b>	<b>2019 €000</b>	2018 €000
Depreciation of property, plant and equipment (note 11)	<b>1,598</b>	1,593
Depreciation of Right of Use assets (note 12)	<b>6,223</b>	–
Amortisation of other intangible assets (note 10)	<b>2,391</b>	2,244
Acquisition related costs	<b>97</b>	115
Staff costs (see note 4)	<b>34,937</b>	32,129

The detailed analysis of auditor's remuneration is provided below:

#### Audit services

Fees payable to the auditor for the audit of these financial statements	<b>46</b>	36
Fees payable to auditor for the audit of the Company's subsidiaries	<b>128</b>	110

#### Total audit fees

	<b>174</b>	146
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#### Non-audit services

Assurance services for review of half-year statement	<b>–</b>	10
IFRS 16 project set-up costs	<b>25</b>	–
Other assurance services for the audit of the Company pension scheme	<b>11</b>	8

#### Total non-audit fees

	<b>36</b>	18
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#### Total fees paid to auditor

	<b>210</b>	164
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2018 fees were paid to the previous auditor KPMG LLP.

The IFRS 16 project set-up costs were incurred in advance of the appointment of Deloitte LLP as auditor and the project was terminated on appointment as auditor, with no reliance being placed on the work undertaken by Deloitte LLP to support the values disclosed in the financial statements. An alternative provider was engaged to support the Group with its IFRS 16 work.

The Audit Committee reviews and approves non-audit work which the auditor performs, including the fees paid for such work, to ensure that the auditor's objectivity and independence is not compromised.



## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 3. Exceptional item 2018

As reported in the 2018 Annual Report, following the High Court judgement involving Lloyds Banking Group in October 2018, the Directors made the judgement that the estimated effect of Guaranteed Minimum Pension ('GMP') equalisation on the Group's pension liabilities was a past service cost for pensionable service between 1990 and 1997 that should be reflected as an exceptional item. Any subsequent change in estimate will be recognised in other comprehensive income. The judgement was based on the fact that pension liabilities for the Group's pension scheme at 31 December 2017 did not include any amounts for GMP equalisation.

Accordingly, an exceptional cost of £330,000 was recognised in the 2018 financial statements as a past service cost in respect of the equalisation of GMP benefits. We believe that this classification as an exceptional cost provides a more meaningful basis for measuring financial performance.

It is expected that there will be follow-on court hearings to further clarify the application of GMP equalisation in practice and there may yet be appeals against all or part of the judgement. Whilst the 2018 financial statements reflected our best estimate of the impact on pension liabilities, the estimate involved a number of assumptions. As the outcome of future court hearings cannot be reliably predicted, the estimate continues to reflect the information currently available. The Directors will continue to monitor any clarifications or developments and consider the impact on pension liabilities.

The impact on key performance measures in the 2018 consolidated income statement is shown below. Tax on the exceptional item was charged at 17% reflecting the impact of the adjustment on the related deferred tax asset.

	2018 Before exceptional item £000	Exceptional item £000	2018 £000
<b>Operating profit</b>	12,025	(330)	<b>11,695</b>
Finance costs	(809)	–	<b>(809)</b>
<b>Profit before tax</b>	11,216	(330)	<b>10,886</b>
Tax	(2,201)	56	<b>(2,145)</b>
<b>Profit for the year</b>	9,015	(274)	<b>8,741</b>
<b>Earnings per share</b>			
Basic and diluted	5.72p	(0.17p)	<b>5.55p</b>

### 4. Staff costs

<b>The average monthly number of employees (including Directors) was:</b>	2019 No.	2018 No.
Production	<b>190</b>	186
Sales and distribution	<b>496</b>	476
Administration	<b>247</b>	233
	<b>933</b>	895

<b>The costs incurred in respect of these employees were:</b>	2019 £000	2018 £000
Wages and salaries	<b>30,311</b>	27,791
Social security costs	<b>2,860</b>	2,621
Pension costs		
Contributions to defined contribution schemes	<b>1,579</b>	1,597
Contributions to defined benefit schemes	<b>112</b>	120
Share-based payments (note 26)	<b>75</b>	–
	<b>34,937</b>	32,129

## 5. Finance costs

	2019 £000	2018 £000
Interest on bank borrowings	573	530
Interest on leases	802	17
Finance cost relating to defined benefit scheme (note 25)	231	262
<b>Finance costs</b>	<b>1,606</b>	809

Interest on leases in 2019 includes the interest on all leases following the transition to IFRS 16 'Leases' as set out in note 18.

Interest in 2018 only includes the interest on finance leases under IAS 17 'Leases'.

## 6. Tax

	2019 £000	2018 £000
<b>Current tax</b>		
United Kingdom corporation tax	2,057	1,953
Foreign tax	104	98
Adjustments in respect of prior years	(53)	(42)
<b>Current tax charge</b>	<b>2,108</b>	2,009
<b>Deferred tax</b>		
Current year	185	136
<b>Deferred tax charge</b> (see note 19)	<b>185</b>	136
<b>Total tax charge</b>	<b>2,293</b>	2,145

The standard rate of tax based on the UK average rate of corporation tax is 19.0%. Taxation for other jurisdictions is calculated at the rates prevailing in these jurisdictions.

The actual tax charge varies from the standard rate of tax on the results in the consolidated income statement for the reasons set out below.

	2019 £000	2018 £000
<b>Profit before tax</b>	<b>12,024</b>	10,886
<b>Tax on profit at 19.0%</b> (2018: 19.0%)	<b>2,285</b>	2,068
<b>Factors affecting tax charge for the year:</b>		
Non-deductible expenses	47	107
Difference on overseas tax rates	14	12
Changes in estimates related to prior years	(53)	(42)
<b>Tax charge for the year</b>	<b>2,293</b>	2,145
<b>Weighted average effective tax rate for the year</b>	<b>19.1%</b>	19.7%

Macfarlane Group's corporate tax structure is such that the effective corporation tax rate should be relatively close to the prevailing tax rate with non-deductible expenses usually the principal reason for any variation.

A reduction in the UK corporation tax rate to 17%, effective from 1 April 2020, was substantively enacted on 6 September 2017. This will reduce the Company's future tax charges. Deferred tax assets and liabilities at 31 December 2019 have been calculated based on the rate of 17% enacted at the balance sheet date.

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 7. Profit for the year

The Company has taken advantage of Section 408 of the Companies Act 2006 and consequently a separate profit and loss account for the parent company is not presented as part of these financial statements.

The Company's profit for the year is disclosed in note 38 to these financial statements.

### 8. Dividends

	2019 £000	2018 £000
<b>Amounts recognised as distributions to equity holders in the year:</b>		
Final dividend for 2018 of 1.65p per share (2017: 1.50p per share)	2,600	2,363
Interim dividend for 2019 of 0.69p per share (2018: 0.65p per share)	1,089	1,024
	<b>3,689</b>	3,387

A proposed dividend of 1.76p per share will be paid on 4 June 2020 to those shareholders on the register at 15 May 2020.

This is subject to approval by shareholders at the Annual General Meeting on 12 May 2020 and therefore has not been included as a liability in these financial statements.

### 9. Earnings per share

	2019 £000	2018 £000
<b>Earnings for the purposes of calculating earnings per share</b>		
Profit for the year before exceptional items	9,731	9,015
Profit for the year	9,731	8,741
<b>Number of shares in issue</b>	<b>2019 Number of shares '000</b>	2018 Number of shares '000
Weighted average number of shares in issue for the purposes of calculating basic earnings per share	157,636	157,548
Effect of Long-Term Incentive Plan awards in issue	393	–
Weighted average number of shares in issue for the purposes of calculating diluted earnings per share	158,029	157,548
<b>Basic earnings per share – before exceptional item</b>	<b>6.17p</b>	5.72p
<b>Basic earnings per share – after exceptional item</b> (see note 3)	<b>6.16p</b>	5.55p
<b>Diluted earnings per share – before exceptional item</b>	<b>6.17p</b>	5.72p
<b>Diluted earnings per share – after exceptional item</b> (see note 3)	<b>6.16p</b>	5.55p

## 10. Goodwill and other intangible assets

	Packaging Distribution £000	Manufacturing Operations £000	2019 Total £000	2018 Total £000
Goodwill	43,944	1,359	45,303	42,210
Other intangible assets	17,360	–	17,360	16,438
<b>Goodwill and other intangible assets</b>	<b>61,304</b>	<b>1,359</b>	<b>62,663</b>	58,648

	Packaging Distribution £000	Manufacturing Operations £000	2019 Total £000	2018 Total £000
<b>Goodwill</b>				
<b>Fair value on acquisition</b>				
<b>At 1 January</b>	<b>40,851</b>	<b>1,359</b>	<b>42,210</b>	40,664
Additions (note 24)	3,093	–	3,093	1,546
At 31 December	43,944	1,359	45,303	42,210
<b>Impairment</b>				
At 1 January and 31 December	–	–	–	–

### Carrying value

<b>At 31 December 2019</b>	<b>43,944</b>	<b>1,359</b>	<b>45,303</b>
At 31 December 2018	40,851	1,359	42,210

On 2 May 2019 the Group's subsidiary, Macfarlane Group UK Limited ('MGUK'), acquired the whole issued share capital of Carnweather, the intermediate parent and 100% owner of Ecopac (U.K.) Limited. On 30 August 2019, Macfarlane Group PLC acquired the whole issued share capital of Leyland Packaging Company (Lancs) Limited. For both acquisitions, goodwill arising on acquisition was added to the Packaging Distribution CGU grouping.

During 2018 MGUK, acquired the whole issued share capital of Tyler Packaging (Leicester) Limited and Harrisons Packaging Limited, with goodwill on acquisition added to the Packaging Distribution CGU grouping.

At 31 December 2019, the Group had two CGU groupings to which goodwill had been ascribed namely:

- (i) Packaging Distribution, comprising goodwill arising on all acquisitions in this segment since 2001; and
- (ii) Manufacturing Operations, comprising the goodwill arising on Labels' acquisitions, primarily in the Reseal-it business in 2000.

The recoverable amount of each CGU grouping is determined using 'value in use' calculations with key assumptions relating to discount rates, sales growth rates, projected gross margin and overhead costs. A post-tax discount rate of 9.0% (2018: 9.8%) is used for both CGU's reflecting the Group's weighted average cost of capital adjusted for appropriate market risk, which is considered to be the most definitive basis for arriving at a discount rate. The Group believes the risk profiles across the markets in which it operates are not significantly different and has therefore deemed it appropriate to apply the same discount rate to both CGUs. The pre-tax discount rate is 11.1% (2018: 12.1%) for each CGU grouping and the Group's effective tax rate is then applied to give the post-tax discount rate. Sales growth rates of 1%, changes in gross margin and overhead costs are based on our expectation of future performance in the markets in which we operate. These are consistent with our budgets for 2020 and strategic plans for future years. The assumptions are used to extrapolate cash flows for five years after which a terminal value is calculated assuming no inherent growth.

The Directors believe the assumptions used are appropriate. In addition they have conducted a sensitivity analysis to determine the changes in assumptions that would result in an impairment of the carrying value of goodwill. Based on this analysis the Directors believe that any reasonable changes in the key assumptions would maintain a recoverable amount for each CGU grouping that exceeds its carrying value. Therefore at 31 December 2019 no impairment charge is required against the carrying value of goodwill.

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 10. Goodwill and other intangible assets (continued)

Other intangible assets	Brand values £000	Customer relationships £000	2019 Total £000	2018 Total £000
<b>Fair value on acquisition</b>				
<b>At 1 January</b>	<b>806</b>	<b>23,534</b>	<b>24,340</b>	22,228
Additions (note 24)	<b>85</b>	<b>3,228</b>	<b>3,313</b>	2,112
At 31 December	<b>891</b>	<b>26,762</b>	<b>27,653</b>	24,340
<b>Amortisation</b>				
At 1 January	<b>559</b>	<b>7,343</b>	<b>7,902</b>	5,658
Charge for year	<b>164</b>	<b>2,227</b>	<b>2,391</b>	2,244
At 31 December	<b>723</b>	<b>9,570</b>	<b>10,293</b>	7,902
<b>Carrying value</b>				
<b>At 31 December 2019</b>	<b>168</b>	<b>17,192</b>	<b>17,360</b>	
At 31 December 2018	247	16,191		16,438

Other intangible assets comprise separately identifiable intangible assets recognised on the acquisitions of businesses and subsidiary companies in Packaging Distribution between 2014 and 2019. They are recorded at fair value on acquisition less subsequent amortisation.

These are primarily Brand values, which are calculated on the Relief from Royalty method and a valuation of Customer relationships, which is calculated on the Excess Earnings method, based on the net anticipated earnings stream. Brand values are calculated on royalty rates of 0.5%, consistent with an assessment of what would be charged in a typical franchise agreement. The valuation of Customer relationships is calculated using our best estimates of customer attrition rates, and returns, based on assessments of performance levels in the markets in which we operate. Brand values and Customer relationship valuations are amortised on a straight-line basis over periods up to five years and over a ten year period respectively.

On 2 May 2019 MGUK acquired the whole issued share capital of Carnweather, the intermediate parent and 100% owner of Ecopac (U.K.) Limited. On 30 August 2019, Macfarlane Group PLC acquired the whole issued share capital of Leyland Packaging Company (Lancs) Limited. For both acquisitions, values for Brand values and Customer relationships within Packaging Distribution were recognised.

At 31 December 2019, the Group retained values in respect of:

Year of acquisition	Company/business acquired	Brand	Customer relationships
2014	Packaging business of Lane Packaging Limited		✓
2014	Network Packaging Limited		✓
2015	Packaging business of One Packaging Limited	✓	✓
2016	Packaging business of Colton Packaging Teesside		✓
2016	Packaging business of Edward McNeil Limited		✓
2016	Nelsons for Cartons & Packaging Limited	✓	✓
2017	Packaging business of Greenwoods Stock Boxes Limited and Nottingham Recycling Limited		✓
2018	Tyler Packaging (Leicester) Limited	✓	✓
2018	Harrisons Packaging Limited	✓	✓
2019	Ecopac (U.K.) Limited	✓	✓
2019	Leyland Packaging Company (Lancs) Limited	✓	✓



## 11. Property, plant and equipment

	Land and buildings £000	Plant and equipment £000	Total £000
<b>Cost</b>			
At 1 January 2018	7,107	26,544	33,651
Acquisitions	–	222	222
Additions	451	1,001	1,452
Disposals	(2)	(531)	(533)
At 1 January 2019	<b>7,556</b>	<b>27,236</b>	<b>34,792</b>
Acquisitions	–	703	703
Additions	557	2,091	2,648
Disposals	(84)	(1,155)	(1,239)
<b>At 31 December 2019</b>	<b>8,029</b>	<b>28,875</b>	<b>36,904</b>
<b>Accumulated depreciation</b>			
At 1 January 2018	3,453	21,568	25,021
Acquisitions	–	137	137
Charge for year	380	1,213	1,593
Disposals	(2)	(490)	(492)
At 1 January 2019	<b>3,831</b>	<b>22,428</b>	<b>26,259</b>
Acquisitions	–	480	480
Charge for year	427	1,171	1,598
Disposals	(77)	(977)	(1,054)
<b>At 31 December 2019</b>	<b>4,181</b>	<b>23,102</b>	<b>27,283</b>
<b>Carrying amount</b>			
<b>At 31 December 2019</b>	<b>3,848</b>	<b>5,773</b>	<b>9,621</b>
At 31 December 2018	3,725	4,808	8,533
At 31 December 2017	3,654	4,976	8,630

The main components of property, plant and equipment are:

- (i) Three properties owned by the Group in Manufacturing Operations and tenant's improvements at a number of short and medium-term leases in Packaging Distribution, categorised as Land and buildings.
- (ii) A significant investment in plant and machinery in Manufacturing Operations, typically printing presses in our Labels' businesses and corrugated case-making machinery in our Packaging Design and Manufacture business as well as investments in our IT hardware system in the Packaging Distribution and Packaging Design and Manufacture businesses, which are all categorised under the combined heading of Plant and equipment.

	2019 £000	2018 £000
<b>Land and buildings at net book value comprise:</b>		
Freeholds	<b>1,830</b>	1,868
Long leaseholds	<b>1,688</b>	1,201
Short leaseholds	<b>330</b>	656
	<b>3,848</b>	3,725

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 12. Right of use assets

	Property £000	Plant, machinery & vehicles £000	Total £000
<b>Cost</b>			
On adoption of IFRS 16 on 1 January 2019	22,725	4,751	27,476
Acquisitions	967	12	979
Additions	1,926	1,697	3,623
<b>At 31 December 2019</b>	<b>25,618</b>	<b>6,460</b>	<b>32,078</b>
<b>Accumulated depreciation</b>			
Charge for year	4,707	1,516	6,223
<b>At 31 December 2019</b>	<b>4,707</b>	<b>1,516</b>	<b>6,223</b>
<b>Carrying amount</b>			
<b>At 31 December 2019</b>	<b>20,911</b>	<b>4,944</b>	<b>25,855</b>

The property portfolio in the Packaging Distribution business comprises a number of property leases for periods of between one year and ten years. The majority of the property arrangements are subject to rent reviews. In addition the Group leases the majority of its commercial vehicles, motor vehicles and forklift trucks on leasing arrangements, which run for periods of up to six years.

Following the adoption of IFRS 16 'Leases' on 1 January 2019, these leases now incorporate values for Right of Use assets. Additional details are set out in the accounting policies and note 18 Lease liabilities.

### 13. Subsidiary companies

Subsidiary companies, with names, countries of incorporation and registered offices, are shown on page 108.

The Group has agreed to exempt the three companies, Harrison's Packaging Limited (Company number 06999588), Leyland Packaging Company (Lancs) Limited (Company number 03775077) and Tyler Packaging (Leicester) Limited (Company number 03460830) from the provisions of the Companies Act relating to the audit of individual accounts by virtue of section 479A.

### 14. Inventories

	2019 £000	2018 £000
Raw materials and consumables	710	842
Work in progress	204	288
Finished goods and goods for resale	14,899	15,810
	<b>15,813</b>	16,940

Inventories represent raw materials, work in progress and finished goods held at the year-end in each of the Group's businesses to respond to customers' requirements for product.

	2019 £000	2018 £000
Cost of inventories recognised as an expense in the consolidated income statement	<b>149,014</b>	146,687

Inventories recorded in the Group's balance sheet comprise large numbers of comparatively small balances. Local teams review inventory levels, older and obsolete inventories and provide against exposures throughout the year. The Group's executive management then reviews these local judgements to ensure they properly reflect movements in absolute inventory levels, ageing of holdings and known obsolescence.

<b>Movement in the provisions for slow-moving and obsolete inventories</b>	<b>2019 £000</b>	2018 £000
At 1 January	<b>448</b>	691
Acquisitions	<b>187</b>	—
Additional provisions recognised in the consolidated income statement	<b>545</b>	626
Inventory written off during the year	<b>(467)</b>	(869)
<b>At 31 December</b>	<b>713</b>	448

## 15. Trade and other receivables

	<b>2019 £000</b>	2018 £000
<b>Current</b>		
Trade receivables	<b>47,005</b>	46,539
Loss allowance	<b>(310)</b>	(304)
	<b>46,695</b>	46,235
Lease receivables	<b>246</b>	—
Other receivables	<b>2,571</b>	2,952
Prepayments and accrued income	<b>2,532</b>	2,173
	<b>52,044</b>	51,360
<b>Non-current</b>		
Other receivables	<b>35</b>	162

Trade receivables represent amounts owed by customers in respect of the revenue for goods or services provided to customers by Macfarlane Group prior to the year end. The Group's credit risk is primarily attributable to its trade receivables. The average credit period taken on sales of goods at the reporting date is 57 days (2018: 59 days). No interest is charged on overdue receivables.

The Group uses external credit scoring systems to assess new customers' credit quality and this determines the credit limits for each customer. The Group has a substantial customer base covering a wide range of customer segments. No individual customer represents more than 5% of the total receivables balance. Receivables balances > £25,000 are reviewed by the Board twice in each year.

Since the inception of IFRS 9 'Financial Instruments', Macfarlane Group has applied a simplified approach to measuring ECL, using a provision matrix which takes into account historical credit loss experience based on the past due status of receivables, adjusted as appropriate to reflect current conditions and management's estimates of future economic conditions and known recoverability issues as a means of measuring the loss allowance for trade receivables carried in the balance sheet at each reporting date.

The Group writes off trade receivables when there is no realistic prospect of recovery of the receivable. The amount is written off against the loss allowance held. The credit risk profile of these receivables is presented based on their past due status and the calculated loss ratios applied to the profiled receivables to give the ECL.

<b>Risk profile category (ageing)</b>	<b>2019 £000</b>	<b>ECL rate</b>	<b>2019 ECL allowance</b>	2018 £000	ECL rate	2018 ECL allowance
Current	<b>34,751</b>	<b>0.37%</b>	<b>130</b>	32,537	0.42%	137
<b>Overdue</b>						
0-30 days	<b>6,381</b>	<b>0.75%</b>	<b>48</b>	7,341	0.81%	59
30-60 days	<b>4,534</b>	<b>1.04%</b>	<b>47</b>	5,729	1.12%	64
60-90 days	<b>1,061</b>	<b>3.11%</b>	<b>33</b>	857	3.37%	29
Over 90 days	<b>278</b>	<b>18.67%</b>	<b>52</b>	75	20.25%	15
	<b>47,005</b>		<b>310</b>	46,539		304

The level of loss allowance has remained steady within a range of 0.66% and 0.75% of the gross value of trade receivables. Amounts in the balance sheet are shown net of the allowance for trade receivables of £310,000 (2018: £304,000). The ECL values reflect the Group's prior experience and assessment of the current economic environment. In determining the recoverability of trade receivables and the level of loss allowance, known changes in credit quality or expected credit loss from the date credit was originally granted are taken into account.

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 15. Trade and other receivables (continued)

	2019 £000	2018 £000
<b>Loss allowance</b>		
At 1 January	304	361
Change in loss allowance for new trade receivables in 2019	203	181
Amounts written off as uncollectible (net of recoveries)	(197)	(238)
<b>At 31 December</b>	<b>310</b>	304

The Directors consider that the carrying amount of Trade and Other Receivables approximate to their fair value.

### 16. Financial instruments

The Group funds its operations from a number of sources of finance, namely operating cash flow, bank borrowings, finance lease borrowings and shareholders' equity, comprising share capital, reserves and retained earnings. The objective is to achieve a capital structure with an appropriate cost of capital, whilst providing flexibility in immediate and medium-term funding to accommodate any material investment requirements.

The Group's principal financial instruments comprise borrowings, cash and short-term deposits, and other items, such as trade receivables and trade payables that arise directly from its operations. The main purpose of these financial instruments is to provide finance for the Group's operations. Throughout the period under review, the Group's policy is that no trading in financial instruments is undertaken for speculative purposes.

There has been no significant change to the Group's exposure to market risks during 2019. Principal risks arising are liquidity risk and credit risk, with secondary risks being interest rate risk and currency risk. The Board reviews and agrees policies for managing each of these risks, which are summarised below and have remained unchanged since the beginning of 2020.

#### Liquidity risk

The Group's liquidity requirements are met by ensuring adequate access to funds by maintaining appropriate levels of committed bank facilities, which are reviewed regularly. The principal Group bank borrowing facility with Lloyds Banking Group PLC of £30 million is available until June 2022. The facility bears interest at normal commercial rates and carries standard financial covenants in relation to interest cover and levels of headroom relative to certain trade receivables' balances. The maturity profile of debt outstanding at 31 December 2019 is set out in this note to the financial statements.

#### Credit risk

The Group's exposure to credit risk is managed by dealing only with banks and financial institutions with good credit ratings and by applying considerable rigour in managing trade receivables. The Group's principal credit risk is primarily attributable to its trade receivables. Amounts presented in the balance sheet are shown net of an ECL allowance, as estimated by the Group's management with details set out in note 15.

#### Interest rate risk

The Group finances its business through a mixture of equity and bank borrowings. The Group borrows in the desired currencies at floating rates of interest. It was not considered necessary to cover interest rate exposures by the use of financial instruments during 2019.

A sensitivity analysis has been prepared based on bank interest rate exposures at the year-end date and the stipulated change taking place at the beginning of the financial year and held constant throughout the year. If interest rates had been 50 basis points higher and all other variables held constant, the Group's profit before tax would have decreased by £96,000 (2018: £84,000).

#### Currency risk

The Group has two overseas subsidiaries, one operating in Ireland and the other operating in Sweden. Revenues and expenses are denominated exclusively in Euros and Swedish Krone respectively. As a result, movements in the Euro and Swedish Krone to Sterling exchange rates could affect the Group's Sterling balance sheet. The Group's policy during 2019 has been to review the need to hedge currency exposures on a regular basis and it was not considered necessary to cover existing currency exposures by the use of financial instruments. The Group continues to review the need to hedge exposures on a regular basis.

The Sterling value of foreign currency denominated assets and liabilities at the year-end is as follows:

	<b>Assets 2019 £000</b>	Assets 2018 £000	<b>Liabilities 2019 £000</b>	Liabilities 2018 £000
Euros	<b>4,955</b>	1,912	<b>4,277</b>	1,150
Swedish Krone	<b>633</b>	1,302	<b>253</b>	891
	<b>5,588</b>	3,214	<b>4,530</b>	2,041

The Sterling value of the Group's foreign currency denominated profit/(loss) before tax is as follows:

	<b>2019 £000</b>	2018 £000
Euros	<b>(47)</b>	(72)
Swedish Krone	<b>472</b>	444
	<b>425</b>	372

The following table details the sensitivity to a 5% reduction in Sterling against the respective foreign currencies. The sensitivity of the Group's exposure to foreign currency risk is determined based on the exposure at the year-end and on the change taking place at the beginning of the financial year and held constant throughout the year.

	<b>Result 2019 £000</b>	Result 2018 £000	<b>Other equity 2019 £000</b>	Other equity 2018 £000
Euros	<b>(2)</b>	(3)	<b>34</b>	38
Swedish Krone	<b>23</b>	22	<b>19</b>	21
	<b>21</b>	19	<b>53</b>	59

	<b>2019 £000</b>	2018 £000
<b>Cash and cash equivalents</b>		
<b>Currency</b>		
Sterling	<b>2,785</b>	4,129
Euros	<b>370</b>	469
US Dollars	<b>54</b>	–
Swedish Krone	<b>101</b>	13
<b>Cash and cash equivalents</b>	<b>3,310</b>	4,611
<b>Bank borrowings and loans</b>		
Currency – Sterling	<b>15,984</b>	17,769
<b>Bank borrowings and loans</b>	<b>15,984</b>	17,769
<b>Net bank debt</b>	<b>12,674</b>	13,158

Cash and cash equivalents set out above comprise cash at bank and other short-term highly liquid investments with maturity of three months or less.

The principal Group bank borrowing facility with Lloyds Banking Group PLC ('Lloyds') of £30 million is available until June 2022. Under the facility, the trade receivables of the Group's largest trading subsidiary, Macfarlane Group UK Limited have been assigned to Lloyds who then fund the Group in advance of the collection of the transferred receivables. The Invoice Discounting facility bears interest at normal commercial rates and carries standard financial covenants in relation to interest cover and levels of headroom relative to certain trade receivables' balances. The Group is currently in compliance with all conditions in relation to its borrowing facility.

### Interest rates

All Group borrowings are held at floating rates of interest. The average effective interest rate on bank borrowings approximates to 2.80% per annum (2018: 2.65%).



## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 16. Financial instruments (continued)

#### Fair value of financial instruments

Current assets and liabilities are all held at floating rates. The fair values of cash and cash equivalents and bank borrowings at 31 December 2019 all materially equate to book values.

#### Borrowing facilities

The Group has committed borrowing facilities available at 31 December 2019, in respect of which all conditions precedent had been met, as follows:

	2019 £000	2018 £000
Drawn down	15,984	17,769
Undrawn	14,016	12,231
<b>Committed borrowing facilities</b>	<b>30,000</b>	30,000

The principal Group borrowing facility of £30 million (2018: £30 million) is with Lloyds Banking Group PLC.

The Group's borrowing profile is as follows:	2019 £000	2018 £000
<b>At amortised cost</b>		
Bank borrowings – secured	15,984	17,769
Lease liabilities	6,321	101
<b>Current borrowings</b>	<b>22,305</b>	17,870
Non-current – lease liabilities	19,646	–
<b>Total borrowings</b>	<b>41,951</b>	17,870
<b>Equity</b>	<b>69,271</b>	62,532
<b>Gearing (net debt to equity) ratio</b>	<b>61%</b>	29%

#### Financial instruments carried at fair value

IFRS 7 requires that all financial instruments carried at fair value be analysed under certain levels. The table below analyses financial instruments, into a fair value hierarchy based on the valuation technique used to determine fair value.

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The fair values of all financial assets and financial liabilities by class together with their carrying amounts shown in the balance sheet are as follows:

Financial assets designated at fair value through profit or loss (note 17)	Carrying amount 2019 £000	Fair value 2019 £000	Level 1 2019 £000	Level 2 2019 £000	Level 3 2019 £000
Contingent consideration	1,600	1,600	–	–	1,600
	Carrying amount 2018 £000	Fair value 2018 £000	Level 1 2018 £000	Level 2 2018 £000	Level 3 2018 £000
Contingent consideration	1,600	1,600	–	–	1,600

The following table shows the valuation techniques used for Level 3 fair values, and the significant unobservable inputs used for Level 3 items.

Financial instruments measured at fair value	Valuation technique	Significant unobservable inputs (Level 3 only)
Contingent consideration	The expected payment reflects calculated cash outflows under possible earn-out scenarios and is not discounted	Trading performance of acquired subsidiary companies in the 12 months following acquisition

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the effect of netting agreements.

	2019 Contractual cash flows			
	Total €000	Due < 1 year or less €000	Due 1 to 5 years €000	Due after 5 years €000
<b>Non-derivative financial instruments</b>				
Secured bank borrowings	15,984	15,984	–	–
Lease liabilities	25,967	6,321	16,035	3,611
Trade payables	36,221	36,199	22	–
	<b>78,172</b>	<b>58,504</b>	<b>16,057</b>	<b>3,611</b>

	2018 Contractual cash flows		
	Total €000	Due < 1 year or less €000	Due 1 to 5 years €000
<b>Non-derivative financial instruments</b>			
Secured bank borrowings	17,769	17,769	–
Lease liabilities	101	101	–
Trade payables	37,154	37,129	25
	<b>55,024</b>	<b>54,999</b>	<b>25</b>

## 17. Trade and other payables

	2019 €000	2018 €000
<b>Due within one year</b>		
Trade payables	36,199	37,129
Other taxation and social security	3,662	3,438
Contingent consideration	1,600	1,600
Other creditors	515	810
Accruals and deferred income	6,554	4,914
	<b>48,530</b>	<b>47,891</b>
<b>Due after more than one year</b>		
Other creditors	22	25

Trade and other payables principally comprise amounts outstanding for trade purchases, ongoing distribution costs and administrative expenses in all the Group's businesses, with no interest charged on trade payables. The Directors consider that the carrying amounts for Trade and Other Payables approximate to their fair value.

## 18. Lease liabilities

	2019 €000	2018 €000
<b>Amounts payable under leases</b>		
Within one year	6,321	101
Between one and five years	16,035	–
After more than five years	3,611	–
<b>Present value of lease liabilities</b>	<b>25,967</b>	<b>101</b>
Due for settlement within 12 months (shown within current liabilities)	(6,321)	(101)
Due for settlement after more than 12 months (shown as non-current liabilities)	19,646	–

From 1 January 2019, the Company recognises a right-of-use asset and a corresponding lease liability for all lease arrangements in which it is the lessee, except for short-term leases with a lease term of 12 months or less and leases of low value assets. For these short-term or low value leases, the Company recognises the lease payments as an operating expense in administrative expenses on a straight-line basis over the term of the lease.

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 18. Lease liabilities (continued)

The lease liability is initially measured at the discounted present value of lease payments not paid at the commencement date. The Company remeasures the lease liability whenever the lease term changes or a lease contract is modified and the modification is not accounted for as a separate lease. Other than these remeasurements, lease payments are primarily fixed rather than variable in nature.

The application of IFRS 16 resulted in a decrease in other operating expenses and an increase in depreciation and interest expense compared to IAS 17. For all leases, the Company recognised the following amounts in the consolidated income statement:

	2019 £000
Depreciation on ROU assets	6,223
Interest expense on lease liabilities	810
Expense relating to short-term leases expiring during 2019	895
Expense relating to variable lease payments not included in the lease liability	1,083

The Directors consider that the carrying amounts for lease liabilities approximate to their fair value.

### 19. Deferred tax

	Tax losses/ accelerated capital allowances £000	Other intangible assets £000	Retirement benefit obligations £000	Total £000
At 1 January 2018	166	(2,817)	2,010	(641)
Acquisition (note 24)	(13)	(358)	–	(371)
(Charged)/credited in income statement	(161)	381	(356)	(136)
Credited in other comprehensive income	–	–	6	6
Deferred tax on remeasurement of pension scheme liability	–	–	6	6
At 1 January 2019	(8)	(2,794)	1,660	(1,142)
Acquisition (note 24)	(37)	(562)	–	(599)
(Charged)/credited in income statement	(121)	405	(469)	(185)
Credited in other comprehensive income	–	–	(92)	(92)
Deferred tax on remeasurement of pension scheme liability	–	–	(92)	(92)
<b>At 31 December 2019</b>	<b>(166)</b>	<b>(2,951)</b>	<b>1,099</b>	<b>(2,018)</b>
<b>2019 deferred tax assets</b>				
Due outwith one year	125	–	1,099	1,224
<b>2019 deferred tax liabilities</b>				
Due outwith one year	(291)	(2,951)	–	(3,242)
	<b>(166)</b>	<b>(2,951)</b>	<b>1,099</b>	<b>(2,018)</b>
2018 deferred tax assets				
Due outwith one year	191	–	1,660	1,851
2018 deferred tax liabilities				
Due outwith one year	(199)	(2,794)	–	(2,993)
	(8)	(2,794)	1,660	(1,142)

Deferred tax balances represent the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method.

A reduction in the UK corporation tax rate to 17%, effective from 1 April 2020, was substantively enacted on 6 September 2017. This will reduce the Company's future current tax charge. Deferred tax assets and liabilities at 31 December 2019 and 31 December 2018 have been calculated based on this rate.

## 20. Share capital

	Number of 25p shares	2019 £000	2018 £000
<b>Allotted, issued and fully paid:</b>			
At 1 January	157,547,618	<b>39,387</b>	39,387
Issued during the year	264,382	<b>66</b>	—
<b>At 31 December</b>	<b>157,812,000</b>	<b>39,453</b>	39,387

The Company has one class of ordinary shares, which carry no right to fixed income. Each ordinary share carries one vote in any General Meeting of the Company.

On 5 September 2019, the Company issued 264,382 ordinary shares of 25p each at a value of 94.56p per share as non-cash consideration to the Vendors of Leyland Packaging Company (Lancs) Limited, an effective value of £250,000. The shares were admitted to the Official List of the London Stock Exchange on 5 September 2019.

## 21. Reserves

	Share premium £000	Revaluation reserve £000	Translation reserve £000	Retained earnings £000
Balance at 1 January 2018	12,975	70	299	4,479
Profit for the year	—	—	—	8,741
Dividends paid (see note 8)	—	—	—	(3,387)
Foreign currency translation differences – foreign operations	—	—	(6)	—
Remeasurement of pension scheme liability taken direct to equity	—	—	—	(32)
Deferred tax taken direct to equity	—	—	—	—
Tax on remeasurement	—	—	—	6
<b>Balance at 1 January 2019</b>	<b>12,975</b>	<b>70</b>	<b>293</b>	<b>9,807</b>
Profit for the year	—	—	—	<b>9,731</b>
Dividends paid (see note 8)	—	—	—	<b>(3,689)</b>
Foreign currency translation differences – foreign operations	—	—	<b>(62)</b>	—
Issue of new shares	<b>184</b>	—	—	—
Expenses of share issue	<b>(11)</b>	—	—	—
Share-based payments	—	—	—	<b>75</b>
Remeasurement of pension scheme liability taken direct to equity	—	—	—	<b>537</b>
Deferred tax taken direct to equity	—	—	—	—
Tax on remeasurement	—	—	—	<b>(92)</b>
<b>Balance at 31 December 2019</b>	<b>13,148</b>	<b>70</b>	<b>231</b>	<b>16,369</b>

Exchange differences arising in the consolidated accounts on the retranslation at closing rates of the Group's net investments in foreign subsidiary companies are recorded as movements on the Group's translation reserve.

## 22. Financial commitments

Following the assignment of a property head lease at Coventry in October 2011, the Group provided guarantees for the rentals under the head lease in the event of a default by the assignee. The assignee is the UK subsidiary of a multinational business listed on the New York Stock Exchange. As a result of the assignation, there is a contingent liability of £0.4 million, (2018: £0.9 million) being the sub-lease payments from 1 January 2020 until the conclusion of the head lease in November 2020.

Contractual commitments for capital expenditure for which no provision has been made in the accounts amounted to £Nil (2018: £800,000).

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 23. Notes to the cash flow statement

	2019 £000	2018 £000
<b>Profit before tax</b>	<b>12,024</b>	10,886
Adjustments for:		
Amortisation of intangible assets	<b>2,391</b>	2,244
Depreciation of property, plant and equipment (inc. ROU assets)	<b>7,816</b>	1,593
Loss/(gain) on disposal of property, plant and equipment	<b>5</b>	(32)
Share-based payments	<b>75</b>	–
Finance costs	<b>1,606</b>	809
<b>Operating cash flows before movements in working capital</b>	<b>23,917</b>	15,500
Decrease/(increase) in inventories	<b>2,006</b>	(1,192)
Decrease in receivables	<b>1,178</b>	2,183
(Decrease)/increase in payables	<b>(947)</b>	122
Pension scheme contributions (less current service cost)	<b>(2,994)</b>	(2,352)
<b>Cash generated by operations</b>	<b>23,160</b>	14,261
Income taxes paid	<b>(2,288)</b>	(1,882)
Interest paid	<b>(1,375)</b>	(547)
<b>Net cash inflow from operating activities</b>	<b>19,497</b>	11,832

	Cash and cash equivalents £000	Bank borrowing £000	Lease liabilities £000	Total debt £000
At 1 January 2018	2,013	(16,346)	(342)	(14,675)
Cash movements	2,598	(1,423)	253	1,428
Non-cash movements				
Acquisitions	–	–	(12)	(12)
At 31 December 2018	4,611	(17,769)	(101)	(13,259)
Cash movements	<b>(1,301)</b>	<b>1,785</b>	<b>6,699</b>	<b>7,183</b>
Non-cash movements				
IFRS 16 transition on 1 January 2019	–	–	<b>(27,963)</b>	<b>(27,963)</b>
New leases	–	–	<b>(3,623)</b>	<b>(3,623)</b>
Acquisitions	–	–	<b>(979)</b>	<b>(979)</b>
At 31 December 2019	<b>3,310</b>	<b>(15,984)</b>	<b>(25,967)</b>	<b>(38,641)</b>
<b>Net bank debt 2019</b>	<b>3,310</b>	<b>(15,984)</b>		<b>(12,674)</b>
Net bank debt 2018	4,611	(17,769)		(13,158)

Cash and cash equivalents (presented as a single class of asset on the face of the balance sheet) comprise cash at bank and other short-term highly liquid investments with maturity of three months or less.

\* The movement in net debt is inclusive of the net cash outflow in respect of acquisitions set out in note 24.



## 24. Acquisitions

On 2 May 2019, the Group's subsidiary, MGUK acquired 100% of the issued share capital of Carnweather Limited, the parent company of Ecopac, for a maximum consideration of approximately £3.9 million. £3.1 million was paid in cash on acquisition. The deferred consideration of £0.8 million is payable in 2020, subject to certain trading targets being met in the twelve month period ending on 30 April 2020.

On 30 August 2019, Macfarlane Group PLC acquired 100% of the issued share capital of Leyland, for a maximum consideration of approximately £3.05 million. £2.00 million was paid in cash on acquisition with shares to the value of £0.25 million issued to the Vendors on acquisition. Deferred consideration of £0.8 million is payable in 2020, subject to certain trading targets being met in the twelve month period ending on 31 August 2020.

Contingent considerations are recognised as a liability in trade and other payables and are remeasured to fair value of £1.6 million at the balance sheet date based on a range of outcomes between £Nil and £1.6 million. Trading in the post-acquisition periods to 31 December 2019 supports the remeasured value of £1.6 million.

In 2018, MGUK acquired 100% of Tyler for a consideration of approximately £2.1 million. £1.5 million was paid in cash on acquisition, with the deferred consideration of £0.6 million paid in 2019, as trading targets were met in full. In 2018 MGUK also acquired 100% of Harrisons for a maximum consideration of approximately £2.8 million. £1.8 million was paid in cash on acquisition. Of the maximum deferred consideration of £1.0 million, £0.6 million was paid in 2019, reflecting the results in the trading year after acquisition and £0.4 million was released to the income statement.

The impact of the acquisitions on the 2019 results is set out in the Strategic Report on page 8. If the acquisitions had been completed on the first day of 2019, revenues for the year would have been £10.5 million and profit would have been £1.3 million.

All the businesses detailed above are part of the Packaging Distribution segment. Goodwill arising on the acquisitions is attributable to the anticipated future profitability of the distribution of Group product ranges and anticipated operating synergies from future combinations of activities in the Packaging Distribution network.

Fair values assigned to net assets acquired and consideration paid and payable are set out below:

	Carnweather inc. Ecopac (U.K.) £000	Leyland Packaging (Lancs) £000	Previous years' acquisitions £000	2019 Total £000	2018 Total £000
<b>Net assets acquired</b>					
Other intangible assets (note 10)	1,561	1,752	–	<b>3,313</b>	2,112
Property, plant and equipment (inc. ROU assets)	685	509	–	<b>1,194</b>	85
Inventories	395	484	–	<b>879</b>	283
Trade and other receivables	1,196	601	–	<b>1,797</b>	831
Cash and bank balances	211	38	–	<b>249</b>	1,733
Bank borrowings	–	(149)	–	<b>(149)</b>	–
Trade and other payables	(974)	(684)	–	<b>(1,658)</b>	(1,075)
Current tax liabilities	(91)	(144)	–	<b>(235)</b>	(161)
Lease liabilities (inc. IFRS 16 liabilities)	(549)	(430)	–	<b>(979)</b>	(12)
Deferred tax liabilities	(287)	(312)	–	<b>(599)</b>	(371)
<b>Net assets acquired</b>	<b>2,147</b>	<b>1,665</b>	<b>–</b>	<b>3,812</b>	<b>3,425</b>
Goodwill arising on acquisition (note 10)	1,704	1,389	–	<b>3,093</b>	1,546
<b>Total consideration</b>	<b>3,851</b>	<b>3,054</b>	<b>–</b>	<b>6,905</b>	<b>4,971</b>
<b>Contingent consideration on acquisitions</b>					
Current year	(800)	(800)	–	<b>(1,600)</b>	(1,600)
Prior years	–	–	1,207	<b>1,207</b>	4,000
<b>Shares issued for non-cash consideration</b>	<b>–</b>	<b>(250)</b>	<b>–</b>	<b>(250)</b>	<b>–</b>
<b>Total cash consideration</b>	<b>3,051</b>	<b>2,004</b>	<b>1,207</b>	<b>6,262</b>	<b>7,371</b>
<b>Net cash outflow arising on acquisitions</b>					
Cash consideration	(3,051)	(2,004)	(1,207)	<b>(6,262)</b>	(7,371)
Cash and bank balances acquired	211	(111)	–	<b>100</b>	1,733
<b>Net cash outflow – acquisitions</b>	<b>(2,840)</b>	<b>(2,115)</b>	<b>(1,207)</b>	<b>(6,162)</b>	<b>(5,638)</b>

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 25. Retirement benefit obligations

#### Introduction

Macfarlane Group PLC sponsors a defined benefit pension scheme for certain active and former UK employees – the Macfarlane Group PLC Pension & Life Assurance Scheme (1974) ('the Scheme'). Two of the trading subsidiaries, Macfarlane Group UK Limited and Macfarlane Labels Limited are also sponsoring employers of the Scheme. The Scheme is currently in deficit and disclosure of the respective proportions of the Group deficit are included and disclosed in the financial statements of each of the three participating employers.

The Scheme is an HMRC registered pension scheme, administered by a Board of Trustees composed of employer-nominated representatives and member-nominated Trustees which is legally separate from the Group. The Scheme's investments are held separately from those of the Group in managed funds under the supervision of the Trustees. The Trustees are required by law to act in the interest of all classes of beneficiary in the Scheme and are responsible for investment policy and the administration of benefits.

The Scheme provides qualifying employees with an annual pension of 1/60 of pensionable salary for each completed year's service on attainment of a normal retirement age of 65. Pensionable salaries were frozen for the remaining active members at the levels current at 30 April 2009 with the change taking effect from 30 April 2010. As a result no further salary inflation applies for active members who elected to remain in the Scheme. Active members' benefits also include life assurance cover, with the payment of these benefits at the discretion of the Trustees of the Scheme.

The Scheme was closed to new entrants during 2002.

On leaving active service a deferred member's pension is revalued from the time of withdrawal until the pension is drawn. Revaluation in deferment is statutory and since 2010 has been revalued on the Consumer Price Index ('CPI') measure of inflation.

Revaluation of pensions in payment is a blend of fixed increases and inflationary increases depending on the relevant periods of accrual of benefit. For pensions in payment, the inflationary increase is currently based on the Retail Price Index ('RPI') measure of inflation or based on Limited Price Indexation ('LPI') for certain defined periods of service.

During 2012, Macfarlane Group PLC agreed with the Board of Trustees to amend benefits for pensioner, deferred and active members in the Scheme by offering a Pension Increase Exchange ('PIE') option to pensioner members and a PIE option to all deferred and active members at retirement after 1 May 2012.

The Group will consider continued actions to manage and control the deficit in 2020.

#### Balance sheet disclosures at 31 December 2019

The Scheme's qualified actuary from Aon Hewitt carries out triennial valuations using the Projected Unit Credit Method to determine the level of deficit. For the most recent triennial valuation at 1 May 2017, the results of this valuation showed that the market value of the relevant investments of the Scheme was £82,100,000 and represented 81% of the actuarial value of benefits that had accrued to members.

The investment classes held by the Scheme and the Scheme deficit, based on the results of the actuarial valuation as at 1 May 2017, updated to the year-end are as shown below:

Investment class	Valuation 2019 £000	Asset allocation	Valuation 2018 £000	Asset allocation	Valuation 2017 £000	Asset allocation
<b>Equities</b>						
UK equity funds	8,913	10.1%	6,244	8.2%	7,034	8.7%
Overseas equity funds	13,226	15.0%	9,781	12.9%	10,660	13.2%
Multi-asset diversified growth funds	25,382	28.8%	17,512	23.1%	21,533	26.6%
<b>Bonds</b>						
Liability-driven investment funds	27,688	31.5%	28,379	37.4%	28,534	35.2%
<b>Other</b>						
European loan fund	6,379	7.3%	6,645	8.8%	6,562	8.1%
Secured property income fund	6,192	7.0%	7,112	9.4%	6,606	8.2%
Cash	281	0.3%	154	0.2%	31	–
Fair value of scheme investments	88,061	100.0%	75,827	100.0%	80,960	100.0%
Present value of scheme liabilities	(94,526)		(85,592)		(92,783)	
<b>Pension scheme deficit</b>	<b>(6,465)</b>		<b>(9,765)</b>		<b>(11,823)</b>	

The Trustees review the Scheme's investments on a regular basis and consult with the Company regarding any proposed changes to the investment profile. During 2019 adjustments were made between investments to bring the overall allocations into line with the Trustees' strategic asset allocation.

Liability-Driven Investment Funds provide a match of 100% against the impact of movements in inflation on pension liabilities and a match of 85% against the impact of movements in interest rates on pension liabilities.

The ability to realise the Scheme's investments at, or close to, fair value was considered when setting the investment strategy. 86% of the Scheme's investments can be realised at fair value on a daily or weekly basis. The remaining investments have monthly or quarterly liquidity, however, whilst the income from these helps to meet the Scheme's cash flow needs, they are not expected to be realised at short notice. The present value of the Scheme liabilities is derived from cash flow projections over a long period and is thus inherently uncertain.

### Assumptions

The Scheme's liabilities at 31 December 2019 were calculated on the following bases as required under IAS19:

	2019	2018	2017
Discount rate	<b>2.00%</b>	2.80%	2.50%
Rate of increase in salaries	<b>0.00%</b>	0.00%	0.00%
Rate of increase in pensions in payment	<b>3% or 5%</b>	3% or 5%	3% or 5%
	<b>for fixed increases or 2.95% for LPI. 2.15% post 5 April 2006</b>	for fixed increases or 3.20% for LPI. 2.25% post 5 April 2006	for fixed increases or 3.20% for LPI. 2.25% post 5 April 2006
Spouse's pension assumption			
Pensioner/active and deferred members	<b>70%/80%</b>	70%/80%	70%/80%
PIE take up rate	<b>45%</b>	45%	45%
Inflation assumption (RPI)	<b>3.00%</b>	3.30%	3.30%
Inflation assumption (CPI)	<b>2.10%</b>	2.30%	2.30%
Life expectancy beyond normal retirement age of 65			
Male	<b>23.3</b>	23.5	23.7
Female	<b>25.5</b>	25.7	25.7
Average uplift for GMP service	<b>0.40%</b>	0.40%	N/A

### GMP equalisation

In 2018, the Directors made the judgement that the estimated effect of GMP equalisation on the Group's pension liabilities was a past service cost. The average uplift for GMP service for impacted members was reflected through the consolidated income statement as an exceptional item totalling £330,000 in 2018, with any subsequent changes in the estimate to be recognised in other comprehensive income. This treatment was based on the fact that reported pension liabilities for the scheme as at 31 December 2017 did not include any amount in respect of GMP equalisation.

### Sensitivity to significant assumptions

The Pension scheme exposes the Group to actuarial risks, such as interest rate risk, inflation risk, longevity risk and investment risk. The significant assumptions used for IAS 19 are discount rate, inflation and mortality. If different assumptions were used, then this could have a material effect on the deficit. Assuming all other assumptions are held static then a movement in the following key assumptions would affect the level of the Pension scheme deficit as shown below:

	2019 £000	2018 £000	2017 £000
<b>Assumptions</b>			
Discount rate movement of +0.4%	<b>6,048</b>	5,476	5,940
Inflation rate movement of +0.1%	<b>(482)</b>	(436)	(473)
Mortality movement of +0.1 year in age rating	<b>284</b>	257	278

Positive figures reflect a reduction in scheme liabilities and therefore a reduction in the Pension scheme deficit. The sensitivity information has been prepared using the same method as adopted when updating the results of the 2017 actuarial valuation to the balance sheet date and is consistent with the approach adopted in previous years. The level of sensitivities shown reflect average movements in the assumptions in the last three years.

All of the sensitivity information assumes that the average duration of the scheme's liabilities is seventeen years.

## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 25. Retirement benefit obligations (continued)

UK pension legislation requires that pension schemes are funded prudently. Following the conclusion of the 2017 actuarial valuation, the scheme's trustees agreed with the Company to a deficit recovery period of 7 years. As part of this agreement, the Group reconfirmed its effective unconditional right to a refund of any surplus, based on and in accordance with the terms and conditions of the defined benefit scheme and minimum funding requirements. Accordingly IFRIC 14 does not require an adjustment to the net pension liability.

Macfarlane Group PLC paid deficit reduction contributions of £3,106,000 per annum (inclusive of current service costs and interest of £343,000), which along with investment returns from return-seeking assets is expected to make good the actuarial shortfall by April 2024. The estimated deficit reduction contributions in 2019 will be £3,150,000 (inclusive of estimated service costs and interest of £234,000).

The employer contribution rate for active members is 28.7% of pensionable salary and the employee contribution rate is 7.0% of pensionable salary.

	2019 £000	2018 £000
<b>Movement in the scheme deficit during the year</b>		
At 1 January	(9,765)	(11,823)
Current service costs	(112)	(120)
Past service costs for GMP equalisation (see note 3)	–	(330)
Contributions from sponsoring employers	3,106	2,802
Net finance cost (note 5)	(231)	(262)
Remeasurement of pension scheme liability in the year	537	(32)
<b>At 31 December</b>	<b>(6,465)</b>	<b>(9,765)</b>
<b>Analysis of amounts charged to profit before tax</b>		
Current service cost	(112)	(120)
Past service cost for GMP equalisation	–	(330)
Net finance cost	(231)	(262)
<b>Pension expense charged to profit before tax</b>	<b>(343)</b>	<b>(712)</b>
<b>Analysis of the remeasurement of pension scheme liability recognised in the statement of other comprehensive income</b>		
Return on scheme investments excluding amount shown in interest income	11,154	(4,143)
Changes in assumptions underlying the present value of scheme liabilities	(10,617)	4,111
<b>Remeasurement of the pension scheme liability recognised in the statement of other comprehensive income</b>	<b>537</b>	<b>(32)</b>
<b>Movement in the fair value of scheme investments</b>		
At 1 January	75,827	80,960
Interest income	2,109	1,987
Return on scheme investments (excluding amount shown in interest income)	11,154	(4,143)
Contributions from sponsoring employers	3,106	2,802
Contribution from scheme members	70	72
Benefits paid	(4,205)	(5,851)
<b>At 31 December</b>	<b>88,061</b>	<b>75,827</b>
<b>Movement in the present value of scheme liabilities</b>		
At 1 January	(85,592)	(92,783)
Current service cost	(112)	(120)
Past service cost for GMP equalisation	–	(330)
Interest cost	(2,340)	(2,249)
Contributions from scheme members	(70)	(72)
Changes in assumptions underlying the scheme liabilities	(10,617)	4,111
Benefits paid	4,205	5,851
<b>At 31 December</b>	<b>(94,526)</b>	<b>(85,592)</b>

The total of £10,617,000, (2018: (£4,111,000)) set out on the previous page includes changes arising from scheme experience as well as changes in the underlying assumptions of the defined benefit obligations.

The cumulative amount of actuarial losses recognised in other comprehensive income since the date of transition to IAS 19 on 1 January 2004 is £21,366,000 (2018: £21,903,000).

The history of experience adjustments and actual returns on scheme assets and scheme liabilities is as follows:

	2019 £000	2018 £000	2017 £000	2016 £000	2015 £000
Present value of defined benefit obligations	(94,526)	(85,592)	(92,783)	(92,345)	(79,311)
Fair value of scheme investments	88,061	75,827	80,960	77,808	67,793
<b>Pension scheme deficit</b>	<b>(6,465)</b>	(9,765)	(11,823)	(14,537)	(11,518)
<b>Actual return on scheme investments</b>					
Amount	13,263	(2,156)	5,795	12,080	706
Percentage of scheme investments	15.1%	(2.8%)	7.2%	15.5%	1.0%
<b>Experience adjustment on scheme liabilities</b>					
Amount	(10,617)	4,111	(3,953)	(15,162)	1,769
Percentage of scheme liabilities	(11.2%)	4.8%	(4.3%)	(16.4%)	2.2%
<b>Experience adjustment on scheme investments</b>					
Amount	11,154	(4,143)	3,730	9,610	(1,658)
Percentage of scheme investments	12.7%	(5.5%)	4.6%	12.4%	(2.4%)

### Defined contribution schemes

The Group also operates a number of defined contribution pension arrangements, set up as the Macfarlane Group Personal Pension Plan, including an Auto-enrolment plan. The assets of these plans are held separately from those of the Group in independently administered funds. The pension cost charge represents contributions paid by the Group to these plans and amounted to £1,579,000 (2018: £1,597,000). Contributions amounting to £181,000 (2018: £155,000) were payable to the plans and are included in trade and other payables at 31 December.

## 26. Share-based payments

### Equity-settled long-term incentive plans Movements in PSP awards during the year

	Number of shares 2019	Number of shares 2018
Outstanding at 1 January	–	1,135,280
Awarded during the year	604,270	–
Lapsed during the year	–	(1,135,280)
<b>Outstanding at 31 December</b>	<b>604,270</b>	–

A nil cost option award was granted under The Macfarlane Group PLC Long Term Incentive Plan in May 2019 based on 100% of salary. The performance condition requires EPS in 2021 to be 6.77p-8.12p for 25%-100% of this part of the award to vest, working on a straight-line basis. The awards are also subject to an underpin relating to the Remuneration Committee's view on overall performance in the three-year period to 31 December 2021. No re-setting of the award is allowed. The vesting period is three years and any awards, which vest have a holding period of two years following vesting.

The Group recognised an expense of £75,000 (2018: £Nil) in 2019 relating to equity-settled long-term incentive plan awards on the basis that the awards had an estimated probability of vesting of 65%.

## 27. Post balance sheet event

On 6 January 2020, the Company's subsidiary, Macfarlane Group UK Limited acquired the business, goodwill and selected assets of the packaging distribution business of Armagrip Limited, based in County Durham for a consideration of £0.9 million. The net assets acquired amounted to £0.5 million.



## Notes to the financial statements (continued)

For the year ended 31 December 2019

### 28. Related party transactions

The Group has related party relationships with:

- (i) its subsidiaries, listed on page 108;
- (ii) its Directors who comprise the Group Board; and
- (iii) the Macfarlane Group PLC sponsored pension schemes (see note 25).

Transactions between the Company and its subsidiaries are eliminated on consolidation and are not disclosed.

Key management personnel comprise the Group Board. Their remuneration is set out below in aggregate for each of the categories specified in IAS 24 '*Related Party Disclosures*'.

	<b>2019 £000</b>	2018 £000
Directors' remuneration	<b>953</b>	817
Employer's national insurance contributions	<b>130</b>	113
	<b>1,083</b>	930

Further details of Directors' individual and collective remuneration are set out in the Directors' Remuneration Report on page 35. The details provided in the Directors' Remuneration Report address the Companies Act disclosure requirements relating to Directors' remuneration.

Details of Directors' shareholdings in the Company are shown on page 36 and total dividends of £46,000 were paid in respect of these shareholdings in 2019 (2018: £40,000).

Disclosures in relation to the pension schemes are set out in note 25.

The Directors have considered the implications of IAS 24 '*Related Party Disclosures*' and are satisfied that there are no other related party transactions occurring during the year, which require disclosure other than those already disclosed in these financial statements.

# Company balance sheet

At 31 December 2019

	Note	2019 £000	2018 £000
<b>Non-current assets</b>			
Tangible assets	30	61	38
Right of use assets	31	134	–
Investments	32	29,989	35,391
Deferred tax asset	33	439	664
Debtors	34	31,162	27,603
		<b>61,785</b>	63,696
<b>Current assets</b>			
Debtors	34	3,135	2,803
Cash at bank and in hand		2,615	3
<b>Total current assets</b>		<b>5,750</b>	2,806
Creditors – amounts falling due within one year	35	(1,332)	(1,025)
<b>Net current assets</b>		<b>4,418</b>	1,781
<b>Total assets less current liabilities</b>		<b>66,203</b>	65,477
Creditors – amounts falling due after more than one year	36	(128)	(940)
<b>Net assets excluding pension liability</b>		<b>66,075</b>	64,537
Pension liability	41	(2,586)	(3,908)
<b>Net assets</b>		<b>63,489</b>	60,629
<b>Capital and reserves</b>			
Share capital	37	39,453	39,387
Share premium	38	13,148	12,975
Profit and loss account	38	10,888	8,267
<b>Shareholders' funds</b>	39	<b>63,489</b>	60,629

The accompanying notes are an integral part of this Company balance sheet.

The financial statements of Macfarlane Group PLC, Company registration number SC004221, were approved by the Board of Directors on 27 February 2020 and signed on its behalf by



**Peter D. Atkinson**  
Chief Executive



**John Love**  
Finance Director

## Company statement of changes in equity

For the year ended 31 December 2019

	Note	Share capital £000	Share premium £000	Retained earnings £000	Total £000
At 1 January 2018		39,387	12,975	6,989	59,351
<b>Comprehensive income</b>					
Profit for the year		–	–	4,026	4,026
Remeasurement of pension scheme liability	41	–	–	770	770
Tax on remeasurement of pension scheme liability	33	–	–	(131)	(131)
<b>Total comprehensive income</b>		–	–	4,665	4,665
<b>Transactions with shareholders</b>					
Dividends	8	–	–	(3,387)	(3,387)
<b>Total transactions with shareholders</b>		–	–	(3,387)	(3,387)
At 31 December 2018		<b>39,387</b>	<b>12,975</b>	<b>8,267</b>	<b>60,629</b>
<b>Comprehensive income</b>					
Profit for the year		–	–	<b>5,373</b>	<b>5,373</b>
Remeasurement of pension scheme liability	41	–	–	<b>1,038</b>	<b>1,038</b>
Tax on remeasurement of pension scheme liability	33	–	–	<b>(176)</b>	<b>(176)</b>
<b>Total comprehensive income</b>		–	–	<b>6,235</b>	<b>6,235</b>
<b>Transactions with shareholders</b>					
Dividends	8	–	–	<b>(3,689)</b>	<b>(3,689)</b>
Share-based payments	26	–	–	<b>75</b>	<b>75</b>
Issue of share capital	37,38	<b>66</b>	<b>173</b>	<b>–</b>	<b>239</b>
<b>Total transactions with shareholders</b>		<b>66</b>	<b>173</b>	<b>(3,614)</b>	<b>(3,375)</b>
<b>At 31 December 2019</b>		<b>39,453</b>	<b>13,148</b>	<b>10,888</b>	<b>63,489</b>

The accompanying notes are an integral part of this statement of changes in equity.

# Notes to the Company financial statements

For the year ended 31 December 2019

## 29. Significant accounting policies

Macfarlane Group PLC is a public company listed on the London Stock Exchange, incorporated and domiciled in the United Kingdom and registered in Scotland.

These financial statements were prepared in accordance with Financial Reporting Standard 101 *Reduced Disclosure Framework* ('FRS 101').

In preparing these financial statements, the Company applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards as adopted by the EU ('Adopted IFRSs'), but makes amendments where necessary in order to comply with the Companies Act 2006 and has set out below where advantage of the FRS 101 disclosure exemptions has been taken. In these financial statements, the Company has applied the exemptions available under FRS 101 in respect of the following disclosures:

- (i) Cash flow statement and related notes;
- (ii) Comparative period reconciliations for share capital and tangible assets;
- (iii) Disclosures in respect of transactions with wholly owned subsidiaries;
- (iv) The effects of new but not yet effective IFRSs;
- (v) Disclosures in respect of the compensation of Key Management Personnel; and
- (vi) Disclosures in respect of capital management.

As the consolidated financial statements for Macfarlane Group PLC include the equivalent disclosures, the Company has also applied the exemptions available under FRS 101 in respect of certain disclosures required by:

- (i) IFRS 2 *Share Based Payments* in relation to Group-settled share-based payments;
- (ii) IFRS 3 *Business Combinations* relating to business combinations undertaken by the Company; and
- (iii) IFRS 7 *Financial Instruments*.

The Directors, in their consideration of going concern, have reviewed the Company and Group's future cash flow forecasts and revenue projections, which they believe are based on a prudent assessment of the market and past experience as set out on page 65. After making enquiries, the Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for at least the next twelve months. For this reason they continue to adopt the going concern basis in preparing the financial statements.

### Application of accounting policies

The only major change from the adoption of new IFRS's in 2019 is in respect of the adoption of IFRS 16 'Leases'. This is the first set of financial statements where IFRS 16 'Leases' has been applied, with an initial application date of 1 January 2019. IFRS 16 introduces significant changes to lessee accounting by removing the distinction between operating and finance leases, requiring the recognition of a right-of-use asset and a lease liability at commencement for all leases, except for short-term leases and leases of low value assets.

The financial statements are prepared on the historical cost basis except that certain of the following assets and liabilities are stated at their fair value. The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the preparation of these financial statements.

### Key sources of estimation uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported for assets and liabilities as at the balance sheet date and the amounts reported for revenues and expenses during the year. Due to the nature of estimation, the actual outcomes may well differ from these estimates. No significant judgements have been made in the current or prior year.

The key sources of estimation uncertainty that have a significant effect on the carrying amounts of assets and liabilities are discussed below:

### Retirement benefit obligations

The determination of any defined benefit pension scheme liability is based on assumptions determined with independent actuarial advice. The key assumptions used include discount rate, inflation rate and mortality assumptions, for which a sensitivity analysis for the Group deficit is provided in note 25. The Directors consider that those sensitivities represent reasonable sensitivities which could occur in the next financial year.

### Tangible assets

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Depreciation is calculated on a straight-line basis to write off the cost or valuation of the assets to their estimated residual values over the period of their expected useful lives. The rates of depreciation vary between 2%-5% per annum on property and 7%-25% per annum on plant and equipment. Rates of depreciation are reviewed annually to ensure they remain relevant and residual values are reviewed once in each calendar year.

## Notes to the Company financial statements (continued)

For the year ended 31 December 2019

### 29. Significant accounting policies (continued)

#### Investments

Investments held as fixed assets are stated in note 32 at cost less any provision for impairment.

#### Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities, trade and other debtors, cash and cash equivalents, loans and borrowings, and trade and other creditors.

#### Trade and other debtors

Trade and other debtors are recognised initially at fair value. Subsequent to initial recognition they are measured at amortised cost using the effective interest method, less any impairment losses.

#### Trade and other creditors

Trade and other creditors are recognised initially at fair value. Subsequent to initial recognition they are measured at amortised cost using the effective interest method.

#### Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost using the effective interest method.

#### IFRS 16 'Leases'

The Company now recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases (defined as leases with a lease term of 12 months or less) and leases of low value assets. For these short-term or low value leases, the Company recognises the lease payments as an operating expense disclosed in administrative expenses on a straight-line basis over the term of the lease.

For all other leases, the lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted by using the rate implicit in the lease. If this rate cannot be readily determined, the Company uses its incremental borrowing rate.

Lease liabilities are presented on two separate lines in the balance sheet for liabilities due within one year and liabilities due after more than one year. The lease liability is subsequently measured by increasing the carrying amount to reflect interest on the lease liability (using the effective interest method) and by reducing the liability by payments made. The Company remeasures the lease liability (and adjusts the related right-of-use asset) whenever the lease term has changed or a lease contract is modified and the lease modification is not accounted for as a separate lease. The Company did not make any such adjustments during the period presented.

Right-of-use assets comprise the initial measurement of the corresponding lease liability, lease payments made at, or before, the commencement day and any initial direct costs. They are subsequently measured at cost less accumulated depreciation and impairment losses.

Right-of-use assets are depreciated over the shorter period of lease term and useful life of the underlying asset. If a lease transfers ownership of the underlying asset or the cost of the right-of-use asset reflects that the Company expects to exercise a purchase option, the related right-of-use asset is depreciated over the useful life of the underlying asset. Depreciation starts at the commencement date of the lease.

As a practical expedient, IFRS 16 permits a lessee not to separate non-lease components, and instead account for any lease and associated non-lease components as a single arrangement. The Company has not used this practical expedient and has separated out the non-lease components for its leases. These non-lease components, typically servicing and maintenance costs, have been recognised as an expense on a straight-line basis and disclosed in administrative expenses in the profit and loss account.

#### Approach to transition

The Company has applied IFRS 16 using the modified retrospective approach, without restatement of the comparative information. For leases previously treated as operating leases, the Company has elected to follow the approach in IFRS 16, C8(b)(ii), whereby right of use assets are set equal to the lease liability, adjusted for prepaid or accrued lease payments, including un-amortised lease incentives.

The Company's incremental borrowing rate applied to lease liabilities as at 1 January 2019 is 3.0%.

#### Practical expedients adopted on transition

As part of the adoption of IFRS 16 and application of the modified retrospective approach to transition, the Company elected to use the following practical expedients:

- a single discount rate has been applied to assets with reasonably similar characteristics; and
- hindsight has been used in determining the lease term.



There were no adjustments made to the Company balance sheet at 1 January 2019 on adoption of IFRS16 'Leases'.

The table below presents a reconciliation from operating lease commitments disclosed at 31 December 2018 to lease liabilities recognised at 1 January 2019.

	£000
Operating lease commitments disclosed at 31 December 2018 under IAS 17	6
Short-term lease liabilities expiring within 12 months	(6)
Total lease liabilities recognised at 1 January 2019	–

Movements in lease liabilities during 2019 are set out in note 36.

### Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for management services provided to Group undertakings, net of VAT. Revenue is recognised over time as the related charges are made.

### Financial instruments

Financial assets and financial liabilities are recognised in the Company's balance sheet when the Company becomes a party to the contractual provisions of the instrument.

#### Financial assets

Financial assets, categorised as investments, are recognised and derecognised on the effective date where the purchase or sale of an investment is under a contract whose terms require the delivery of the investment within the timeframe established. They are initially measured at fair value, net of transaction costs except for those financial assets classified at fair value through the income statement, which are initially measured at fair value.

Other financial assets comprise trade and other debtors that have fixed or determinable recoveries and are classified as trade and other debtors. The classification takes account of the nature and purpose of the financial assets and is determined on initial recognition. These are measured at amortised cost less impairment.

Indicators are assessed for the impairment of financial assets at each balance sheet date. Financial assets are impaired when there is objective evidence that as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows have been impacted. For trade and other debtors the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows.

The carrying amount of the financial asset is reduced by the impairment loss.

**Cash and cash equivalents** comprise cash on hand and on demand deposits, readily convertible to a known amount of cash and are subject to insignificant risk of changes in value.

**Financial liabilities and equity instruments** are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements.

Financial liabilities comprise solely other financial liabilities under the terms of IFRS 7. Financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortised cost, with interest expense measured on an effective yield basis.

Equity instruments are any contracts evidencing a residual interest in the assets of the Company after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Derivative financial instruments were not used in the current or preceding financial year.

Contingent consideration classified as a liability will be subsequently re-measured through the income statement under the requirements of the revised IFRS 3.

### Share-based payments

The fair value of share-based payments awards granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period in which the employees become unconditionally entitled to the awards. The fair value of the awards granted is measured using an option valuation model, taking into account the terms and conditions upon which the awards were granted. The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date. For share-based payment awards with non-vesting conditions, the grant date fair value of the share-based payment is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes. Details of the determination of the fair value of equity-settled share-based transactions are set out in note 26.

## Notes to the Company financial statements (continued)

For the year ended 31 December 2019

### 29. Significant accounting policies (continued)

#### Taxation

The tax expense represents the sum of the current tax payable and deferred tax.

Current tax is payable based on the taxable profit for the year. Taxable profit differs from profit before tax as reported in the profit and loss account because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The current tax liability is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax balances represent the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised based on tax laws and rates that have been substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying value of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax liabilities are recognised for all taxable temporary differences.

Deferred tax is charged or credited in the profit and loss account, except when it relates to items charged or credited in other comprehensive income, in which case the deferred tax is also recorded in the statement of other comprehensive income.

#### Retirement benefit costs

##### Defined contribution schemes

A defined contribution plan is a post-employment benefit plan under which the Company pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an expense in the profit and loss account in the periods during which services are rendered by employees.

##### Defined benefit schemes

A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The Group's net retirement benefit obligation in respect of its defined benefit pension plan is calculated by estimating the amount of future benefits that employees have earned in return for their service in current and prior periods. These benefits are then discounted to determine the present value, and the fair values of any plan investments, at bid price, are deducted. The Group determines the net interest on the net retirement benefit obligation for the year by applying the discount rate used to measure the defined benefit obligation at the beginning of the year.

The discount rate is set in consultation with the Company's pension advisers, representing the yield at the reporting date on bonds that have a credit rating of at least AA that have maturity dates approximating to the average duration of the Group's retirement benefit obligations and that are denominated in the currency in which the benefits are expected to be paid.

Remeasurements arising from defined benefit plans comprise actuarial gains and losses, returns on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest). Remeasurements are recognised in the statement of other comprehensive income and all other expenses related to defined benefit plans charged in staff costs in the profit and loss account.

When the benefits of a plan are changed, or when a plan is curtailed, the portion of the changed benefit related to past service by employees, or the gain or loss on curtailment, is recognised immediately in the profit and loss account when the plan amendment or curtailment occurs.

The calculation of the retirement benefit obligations is performed by a qualified actuary using the projected unit credit method. When the calculation results in a benefit to the Group, the recognised asset is limited to the present value of benefits available in the form of any future refunds from the plan or reductions in future contributions and takes into account the adverse effect of the present value of any minimum funding requirements.

The net defined benefit cost of the plan is apportioned to participating entities on the basis of the employment history of scheme members, who are allocated to the relevant subsidiary company, with any remaining unallocated members allocated to the parent company.

### 30. Tangible assets

	Land and buildings £000	Plant and equipment £000	Total £000
<b>Cost</b>			
At 1 January 2019	15	246	261
Additions	–	35	35
Disposals	(15)	(108)	(123)
<b>At 31 December 2019</b>	<b>–</b>	<b>173</b>	<b>173</b>
<b>Depreciation</b>			
At 1 January 2019	14	209	223
Charge for the year	1	7	8
Disposals	(15)	(104)	(119)
<b>At 31 December 2019</b>	<b>–</b>	<b>112</b>	<b>112</b>
<b>Net book value</b>			
<b>At 31 December 2019</b>	<b>–</b>	<b>61</b>	<b>61</b>
At 31 December 2018	1	37	38

### 31. Right of use assets

	2019 £000
<b>Cost</b>	
On adoption of IFRS 16 'Leases' on 1 January 2019	–
Additions	148
<b>At 31 December</b>	<b>148</b>
<b>Depreciation</b>	
Charge for year	14
<b>At 31 December</b>	<b>14</b>
<b>Net book value</b>	
<b>At 31 December</b>	<b>134</b>

The Company entered into a new property lease in 2019 which runs for ten years. Following the adoption of IFRS 16 'Leases' on 1 January 2019, the leases are now accounted for with corresponding values for Right of Use assets under these leases. Additional details are set out in note 29, accounting policies and note 36.

### 32. Investments

	2019 £000	2018 £000
<b>Investment in subsidiaries at cost</b>		
At 1 January	35,391	39,544
Additions	3,054	–
Impaired during the year	(939)	(1,421)
Group dividends	–	(180)
Group transfers	(7,517)	(2,552)
<b>At 31 December</b>	<b>29,989</b>	<b>35,391</b>

On 30 August 2019, Macfarlane Group PLC acquired 100% of the issued share capital of Leyland, for a maximum consideration of approximately £3.05 million. £2.00 million was paid in cash on acquisition with shares to the value of £0.25 million issued to the Vendors on acquisition. Deferred consideration of £0.8 million is payable in 2020, subject to certain trading targets being met in the twelve month period ending on 31 August 2020.

## Notes to the Company financial statements (continued)

For the year ended 31 December 2019

### 32. Investments (continued)

During the year the Company wrote down its investment in National Packaging Group Limited to reflect its current realisable value. The parent company transferred its investment in Network Packaging Limited to Macfarlane Group UK Limited during 2019.

Details of the principal operating subsidiaries are set out on page 108.

### 33. Deferred tax asset

	2019 £000	2018 £000
<b>Deferred tax on pension scheme deficit</b>		
At 1 January	664	804
Charged to reserves	(176)	(131)
Charged to profit and loss account	(49)	(9)
<b>At 31 December</b>	<b>439</b>	664

### 34. Debtors

	2019 £000	2018 £000
<b>Due within one year</b>		
Amounts owed by subsidiary undertakings	2,750	1,500
Other receivables	21	628
Prepayments and accrued income	326	571
Deferred tax asset (see below)	38	104
	<b>3,135</b>	2,803
<b>Deferred tax asset – Corporation tax losses</b>		
At 1 January	104	310
Charged to profit and loss account	(66)	(206)
At 31 December	<b>38</b>	104
	2019 £000	2018 £000
<b>Due after more than one year</b>		
Amounts owed by subsidiary undertakings	<b>31,162</b>	27,603

Amounts owed by subsidiary undertakings attract interest at normal commercial rates.

### 35. Creditors – amounts falling due within one year

	2019 £000	2018 £000
Bank borrowings	–	48
Trade creditors	164	270
Other taxation and social security	10	41
Amounts owed to subsidiary undertakings	21	–
Contingent consideration	800	–
Corporation tax	–	432
Accruals and deferred income	324	234
Amounts due under leases (note 36)	13	–
	<b>1,332</b>	1,025

The Company is a party to the Group bank borrowing facility with Lloyds Banking Group PLC, a committed facility of £30 million available until June 2022. The facility bears interest at normal commercial rates and carries standard financial covenants in relation to interest cover and levels of headroom over the trade receivables of Macfarlane Group UK Limited, the principal trading subsidiary.

The Company and certain subsidiaries have given inter-company guarantees to secure the drawdown on this facility. The drawdown at 31 December 2019 by the subsidiary company, Macfarlane Group UK Limited amounted to £15.7 million (2018: £17.8 million).

### 36. Creditors – amounts falling due after more than one year

	2019 £000	2018 £000
Amounts owed to subsidiary undertakings	–	940
Amounts due under leases	128	–
	128	940
<b>Amounts due under leases</b>		
Within one year	13	
Between one and five years	59	
After more than five years	69	
Total amount due	141	
Due within one year	(13)	
Due after more than one year	128	
New leases entered into during 2019	148	
Repayments under leases	(7)	
<b>At 31 December</b>	<b>141</b>	

From 1 January 2019, the Company recognises a right-of-use asset and a corresponding lease liability for all lease arrangements in which it is the lessee, except for short-term leases with a lease term of 12 months or less and leases of low value assets. For these short-term or low value leases, the Company recognises the lease payments as an operating expense disclosed in administrative expenses on a straight-line basis over the term of the lease.

The lease liability is initially measured at the discounted present value of lease payments not paid at the commencement date. The Company remeasures the lease liability whenever the lease term changes or a lease contract is modified and the modification is not accounted for as a separate lease. Other than these remeasurements, lease payments are primarily fixed rather than variable in nature.

### 37. Share capital

	Number of 25p shares	2019 £000	2018 £000
<b>Called up, allotted and fully paid:</b>			
At 1 January	157,547,618	39,387	39,387
Issued during the year	264,382	66	–
<b>At 31 December</b>	<b>157,812,000</b>	<b>39,453</b>	<b>39,387</b>

The Company has one class of ordinary shares, which carry no right to fixed income. Each ordinary share carries one vote in any General Meeting of the Company. On 5 September 2019, the Company issued 264,382 ordinary shares of 25p each at a value of 94.56p per share as non-cash consideration to the Vendors of Leyland Packaging Company (Lancs) Limited, an effective value of £250,000. The shares were admitted to the Official List of the London Stock Exchange on 5 September 2019.



## Notes to the Company financial statements (continued)

For the year ended 31 December 2019

### 38. Reserves

	Share premium £000	Profit and loss account £000	Total £000
Balance at 1 January 2018	12,975	6,989	19,964
Profit for the year	–	4,026	4,026
Dividends paid (note 8)	–	(3,387)	(3,387)
Post-tax actuarial gain in pension scheme taken direct to reserves	–	639	639
Balance at 1 January 2019	<b>12,975</b>	<b>8,267</b>	<b>21,242</b>
Profit for the year	–	<b>5,373</b>	<b>5,373</b>
Dividends paid (note 8)	–	<b>(3,689)</b>	<b>(3,689)</b>
Post-tax actuarial gain in pension scheme taken direct to reserves	–	<b>862</b>	<b>862</b>
Share-based payments (note 26)	–	<b>75</b>	<b>75</b>
Issue of new shares	<b>184</b>	–	<b>184</b>
Expenses of share issue	<b>(11)</b>	–	<b>(11)</b>
<b>Balance at 31 December 2019</b>	<b>13,148</b>	<b>10,888</b>	<b>24,036</b>

### 39. Reconciliation of movements in shareholders' funds

	2019 £000	2018 £000
Profit for the year	<b>5,373</b>	4,026
Dividends to equity holders in the year	<b>(3,689)</b>	(3,387)
Post-tax actuarial gain in pension scheme taken direct to equity	<b>862</b>	639
Share-based payments	<b>75</b>	–
Issue of new shares (net of issue expenses)	<b>239</b>	–
<b>Movements in shareholders' funds in the year</b>	<b>2,860</b>	1,278
Opening shareholders' funds	<b>60,629</b>	59,351
<b>Closing shareholders' funds</b>	<b>63,489</b>	60,629

### 40. Operating profit

	2019 £000	2018 £000
<b>Operating profit for the parent company has been arrived at after charging:</b>		
Depreciation	<b>8</b>	–
Depreciation on Right of Use assets	<b>14</b>	–
Auditor's remuneration – Audit services	<b>46</b>	6
Non-audit services	<b>36</b>	12
<b>Exceptional item</b>		
Past service cost for equalisation of GMP benefits (note 41)	–	132

	2019 No.	2018 No.
<b>Staff costs</b>		
<b>The average monthly number of employees was:</b>		
Administration	<b>10</b>	11

	2019 £000	2018 £000
<b>The costs incurred in respect of these employees were:</b>		
Wages and salaries	<b>1,092</b>	909
Social security costs	<b>144</b>	118
Other pension costs	<b>25</b>	23
Share-based payments (note 26)	<b>75</b>	–
	<b>1,336</b>	1,050

## 41. Pensions

### Introduction

Macfarlane Group PLC sponsors a defined benefit pension scheme for certain active and former UK employees – the Macfarlane Group PLC Pension & Life Assurance Scheme (1974) ('the Scheme'). Two of the trading subsidiaries, Macfarlane Group UK Limited and Macfarlane Labels Limited are also sponsoring employers of the Scheme. The Scheme is currently in deficit and disclosure of the respective proportions of the Group deficit are included and disclosed in the financial statements of each of the three participating employers.

The Scheme is an HMRC registered pension scheme and is administered by a Board of Trustees composed of employer-nominated representatives and member-nominated Trustees which is legally separate from the Group. The Scheme's investments are held separately from those of the Group in managed funds under the supervision of the Trustees. The Trustees are required by law to act in the interest of all classes of beneficiary in the Scheme and are responsible for investment policy and the administration of benefits.

The Scheme provides qualifying employees with an annual pension of 1/60 of pensionable salary for each completed year's service on attainment of a normal retirement age of 65. Pensionable salaries were frozen for the remaining active members at the levels current at 30 April 2009 with the change taking effect from 30 April 2010. As a result no further salary inflation applies for active members who elected to remain in the Scheme. Active members' benefits also include life assurance cover, albeit the payment of these benefits is at the discretion of the Trustees. The Scheme was closed to new entrants during 2002.

On leaving active service a deferred member's pension is revalued from the time of withdrawal until the pension is drawn. Revaluation in deferment is statutory and since 2010 has been revalued on the Consumer Price Index ('CPI') measure of inflation. Revaluation of pensions in payment is a blend of fixed increases and inflationary increases depending on the relevant periods of accrual of benefit. For pensions in payment, the inflationary increase is currently based on the Retail Price Index ('RPI') measure of inflation or based on Limited Price Indexation ('LPI') for certain defined periods of service.

During 2012, Macfarlane Group PLC agreed with the Board of Trustees to amend benefits for pensioner, deferred and active members in the Scheme by offering a Pension Increase Exchange ('PIE') option to pensioner members and a PIE option to all deferred and active members at retirement after 1 May 2012.

### Balance sheet disclosures at 31 December 2019

The Scheme's qualified actuary from Aon Hewitt carries out triennial valuations using the Projected Unit Credit Method to determine the level of deficit. For the most recent triennial valuation at 1 May 2017, the results of this valuation showed that the market value of the relevant investments of the Scheme was £82,100,000 and represented 81% of the actuarial value of benefits that had accrued to members.

The investments held by the scheme and the Scheme deficit, based on the results of the actuarial valuation as at 1 May 2017, updated to the year-end to reflect amounts attributable to Macfarlane Group PLC, the parent company are as shown below:

Investment class	2019 £000	2018 £000	2017 £000
Equities	8,855	6,410	7,078
Multi-asset diversified funds	10,153	7,005	8,613
Liability-driven investment funds	11,075	11,352	11,414
European loan fund	2,477	2,845	2,624
Secured property income fund	2,552	2,658	2,642
Cash	113	60	12
<b>Fair value of scheme investments</b>	<b>35,225</b>	30,330	32,383
Present value of scheme liabilities	(37,811)	(34,238)	(37,113)
<b>Pension scheme deficit</b>	<b>(2,586)</b>	(3,908)	(4,730)

The Trustees review the Scheme's investments on a regular basis and consult with the Company regarding any proposed changes to the investment profile. During 2019 adjustments were made between investments to bring the overall allocations into line with the Trustees' strategic asset allocation.

Liability-Driven Investment Funds provide a match of 100% against the impact of movements in inflation on pension liabilities and a match of 85% against the impact of movements in interest rates on pension liabilities.

## Notes to the Company financial statements (continued)

For the year ended 31 December 2019

### 41. Pensions (continued)

The ability to realise the Scheme's investments at, or close to, fair value was considered when setting the investment strategy. 86% of the Scheme's investments can be realised at fair value on a daily or weekly basis. The remaining investments have monthly or quarterly liquidity, however, whilst the income from these helps to meet the Scheme's cash flow needs, they are not expected to be realised at short notice. The present value of the Scheme's liabilities is derived from cash flow projections over a long period and is thus inherently uncertain. The Scheme's liabilities at 31 December 2019 were calculated on the following bases as required under FRS17:

Assumptions	2019	2018	2017
Discount rate	<b>3.00%</b>	2.80%	2.50%
Rate of increase in salaries	<b>0.00%</b>	0.00%	0.00%
Rate of increase in pensions in payment	<b>3% or 5% for fixed increases or 2.95% for LPI. 2.15% post 5 April 2006</b>	3% or 5% for fixed increases or 3.20% for LPI. 2.25% post 5 April 2006	3% or 5% for fixed increases or 3.20% for LPI. 2.25% post 5 April 2006
Spouse's pension assumption			
Pensioner/active and deferred members	<b>70%/80%</b>	70%/80%	70%/80%
PIE take up rate	<b>45%</b>	45%	45%
Inflation assumption (RPI)	<b>3.00%</b>	3.30%	3.30%
Inflation assumption (CPI)	<b>2.10%</b>	2.30%	2.30%
Life expectancy beyond normal retirement age of 65			
Male	<b>23.3</b>	23.5	23.7
Female	<b>25.5</b>	25.7	25.7
Average uplift for GMP service	<b>0.40%</b>	0.40%	N/A

In 2018, the Directors made the judgement that the estimated effect of GMP equalisation on the Company's pension liabilities was a past service cost in respect of pensionable service between 1990 and 1997. The average uplift for GMP service for impacted members was reflected through the profit and loss account as an exceptional item totalling £132k in 2018 as set out in note 40, with any subsequent changes in the estimate to be recognised in other comprehensive income. This treatment is based on the fact that the reported pension liabilities for the scheme at 31 December 2017 did not include any amount in respect of GMP equalisation.

Movement in scheme deficit during the year	2019 £000	2018 £000
At 1 January	<b>(3,908)</b>	(4,730)
Current service cost	<b>(11)</b>	(13)
Past service cost for GMP equalisation	<b>–</b>	(132)
Company contributions	<b>388</b>	302
Net finance cost	<b>(93)</b>	(105)
Remeasurement of pension scheme liability in the year	<b>1,038</b>	770
<b>At 31 December</b>	<b>(2,586)</b>	(3,908)
<b>Analysis of amounts charged to operating profit</b>		
Current service cost	<b>(11)</b>	(13)
Past service cost for GMP equalisation	<b>–</b>	(132)
<b>Pension cost charged to operating profit</b>	<b>(11)</b>	(145)
<b>Analysis of amounts charged to other financial charges</b>		
Expected return on pension scheme investments	<b>843</b>	795
Interest cost of pension scheme liabilities	<b>(936)</b>	(900)
<b>Other financial charges</b>	<b>(93)</b>	(105)
<b>Analysis of the remeasurement of the scheme deficit</b>		
Return on scheme assets (excluding amount shown in interest income)	<b>5,336</b>	(817)
Changes in assumptions underlying the present value of the scheme's liabilities	<b>(4,298)</b>	1,587
<b>Remeasurement of the pension scheme deficit</b>	<b>1,038</b>	770

	2019 £000	2018 £000
<b>Movement in the fair value of scheme assets</b>		
At 1 January	30,330	32,383
Interest income	843	795
Return on scheme assets (excluding amounts shown in interest income)	5,336	(817)
Contributions from the Company	388	302
Contributions from scheme members	7	7
Benefits paid	(1,679)	(2,340)
<b>At 31 December</b>	<b>35,225</b>	30,330
<b>Movement in the present value of scheme liabilities</b>		
At 1 January	(34,238)	(37,113)
Service cost	(11)	(13)
Past service cost for GMP equalisation	–	(132)
Interest cost	(936)	(900)
Contributions from scheme members	(7)	(7)
Actuarial (loss)/gain in the year	(4,298)	1,587
Benefits paid	1,679	2,340
<b>At 31 December</b>	<b>(37,811)</b>	(34,238)

The cumulative remeasurement of the pension liability applied against reserves since the transition to IAS 19 on 1 January 2004 is a loss of £1,118,000 (2018: £2,156,000).

	2019 £000	2018 £000	2017 £000	2016 £000	2015 £000
Present value of defined benefit obligations	(37,811)	(34,238)	(37,113)	(36,938)	(31,725)
Fair value of scheme investments	35,225	30,330	32,383	31,123	27,118
<b>Pension scheme deficit</b>	<b>(2,586)</b>	(3,908)	(4,730)	(5,815)	(4,607)
<b>Return on scheme investments</b>	<b>6,179</b>	(22)	3,355	5,599	361
Percentage of scheme investments	17.5%	(0.1%)	10.4%	18.0%	1.3%
<b>Experience adjustment to scheme investments</b>	<b>5,336</b>	(817)	2,529	4,610	(585)
Percentage of scheme investments	15.2%	(2.7%)	7.8%	14.8%	(2.2%)
<b>Experience adjustment on scheme liabilities</b>	<b>(4,298)</b>	1,587	(1,634)	(6,107)	1,464
Percentage of scheme liabilities	(11.4%)	4.6%	(4.4%)	(16.5%)	4.6%

### Defined contribution schemes

The Company also participated in a defined contribution scheme, the Macfarlane Group Personal Pension Plan. Contributions to the plan for the year were £14,000 (2018: £11,000) with no contributions payable to the plan at the balance sheet date.

## 42. Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation in the Group financial statements. The Directors have considered the implications of IAS 24 'Related Party Disclosures' and are satisfied that there are no other related party transactions occurring during the year, which require disclosure, other than those already disclosed in these financial statements.

## Principal operating subsidiaries and related undertakings

Company name	Principal activities	Country of registration
<b>Macfarlane Group UK Limited</b> <sup>1</sup> Coventry Tel: 02476 511511 Grantham Tel: 01476 574747 Westbury Tel: 01373 858555	Supply and distribution of all forms of packaging materials and equipment. Design and manufacture of specialist packaging.	England
<b>Nelsons for Cartons &amp; Packaging Limited</b> <sup>1</sup> Leicester Tel: 0116 2641050	Supply and distribution of all forms of packaging materials and equipment.	England
<b>Harrisons Packaging Limited</b> <sup>1</sup> Leyland Tel: 01772 331780	Supply and distribution of all forms of packaging materials and equipment.	England
<b>Ecopac (U.K.) Limited</b> <sup>1</sup> Aylesbury Tel: 01296 652700	Supply and distribution of all forms of packaging materials and equipment.	England
<b>Leyland Packaging Company (Lancs) Limited</b> <sup>1</sup> Leyland Tel: 01772 622622	Supply and distribution of all forms of packaging materials and equipment.	England
<b>Nottingham Recycling Limited</b> <sup>2</sup> Nottingham Tel: 0115 986 7181	Recovery of waste paper and corrugated board for recycling.	England
<b>Macfarlane Labels Limited</b> <sup>3</sup> Kilmarnock Tel: 01563 525151	Manufacture of high quality printed self-adhesive labels and resealable labelling solutions.	Scotland
<b>Macfarlane Group Ireland (Labels &amp; Packaging) Limited</b> <sup>4</sup> Wicklow Tel: 00 353 1281 0234	Manufacture of high quality printed self-adhesive labels and resealable labelling solutions and supply and distribution of packaging materials and equipment.	Ireland
<b>Macfarlane Group Sweden AB</b> <sup>5</sup> Helsingborg Tel: 00 46 42 13 75 55	Provision of high quality printed self-adhesive labels and resealable labelling solutions.	Sweden
<b>Macfarlane Group B.V.</b> <sup>6</sup> Hoofddorp Tel: 00 31 235689207	Supply and distribution of all forms of packaging materials and equipment.	The Netherlands

All the subsidiaries above are wholly owned either by Macfarlane Group PLC or one of its subsidiary companies and operate in the country of registration. The Group's other related undertakings are the dormant subsidiary undertakings disclosed below. In all cases the Company listed as owner controls 100% of the issued share capital.

Company name	Company number	Country of registration
<b>Owned by Macfarlane Group PLC</b>		
National Packaging Group Limited <sup>1</sup>	01355867	England
Adhesive Labels Limited <sup>1</sup>	00723320	England
<b>Owned by Macfarlane Group UK Limited</b>		
Online Packaging Limited <sup>1</sup>	02903657	England
Macfarlane Packaging Limited <sup>7</sup>	SC041678	Scotland
Abbott's Packaging Limited <sup>1</sup>	00372831	England
Mitchell Packaging Limited <sup>1</sup>	00535311	England
Greenwoods Stock Boxes Limited <sup>7</sup>	SC576825	Scotland
Network Packaging Limited <sup>8</sup>	03400627	England
Tyler Packaging (Leicester) Limited <sup>1</sup>	03460830	England
<b>Owned by Harrisons Packaging Limited</b>		
Temperature Controlled Packaging Limited <sup>1</sup>	06896225	England
<b>Owned by Network Packaging Limited</b>		
Networkpack Limited <sup>8</sup>	07076439	England
<b>Owned by Macfarlane Group Sweden AB</b>		
ReSeal-it Scandinavia <sup>5</sup>	556480-9845	Sweden
Regath HB <sup>5</sup>	969610-8753	Sweden

### Registered offices

<sup>1</sup> Siskin Parkway East, Middlemarch Business Park, Coventry CV3 4PE

<sup>2</sup> Abbeyfield Road, Nottingham NG7 2SX

<sup>3</sup> Bentinck Street, Kilmarnock KA1 4AS

<sup>4</sup> Kilmacullagh, Newtownmountkennedy, Co. Wicklow, Ireland

<sup>5</sup> Kapplöpningsgatan 14, f252 30 Helsingborg, Sweden

<sup>6</sup> Siriusdreef 17, 2132WT Hoofddorp, The Netherlands

<sup>7</sup> 3 Park Gardens, Glasgow G3 7YE

<sup>8</sup> Unit 5, Lanesfield Drive, Spring Road Industrial Estate, Ettingshall, Wolverhampton WV4 6UA



# Financial diary

## Financial results

Interim: Announced – August

Final: Announced – February

## Accounts and Annual General Meeting

Report and financial statements – Posted to shareholders on 3 April 2020

Annual General Meeting – Held in Glasgow on 12 May 2020

## Shareholder enquiries

Macfarlane Group PLC's ordinary shares are classified under the 'Industrial – General' section of the Industrial Sector on the London Stock Exchange.

Enquiries regarding shareholdings, dividend payments, dividend mandate instructions, lost share certificates, tax vouchers, changes of address, transfers of shares to another person and other administrative matters should be addressed to the Company's registrars,

Equiniti  
Aspect House  
Spencer Road  
Lancing  
West Sussex, BN99 6DA

Telephone: 0371 384 2439

Website: [www.shareview.co.uk](http://www.shareview.co.uk)

The Company's website, [www.macfarlanegroup.com](http://www.macfarlanegroup.com) provides details of all major Stock Exchange announcements, details of the current share price and information about Macfarlane Group's business.



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