

DIPLOMA PLC



Consistently
delivering
value



Diploma PLC
Annual Report & Accounts 2019

Consistent and sustainable shareholder value creation

Life Sciences

 See pages 12–15

Seals

 See pages 16–19

Controls

 See pages 20–23

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IFC Diploma Model

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Our purpose is to consistently deliver value, empowering our people to service our customers and reward our stakeholders every day

Diploma's strong and successful distribution business model is developed around the proposition of Essential Products, Essential Solutions and Essential Values. The Essential Products that are distributed are critical to customers' needs. The Essential Solutions – deep technical support in Life Sciences, responsive customer service in Seals and value-add servicing in Controls – differentiate the Group from its competitors and drive customer loyalty. The Essential Values focus on empowering our employees, who are best placed to understand and deliver to their customers' needs

The Group's value-add distribution model is built on strong foundations and supported by its Core Competencies and Organisational Capability

The Group will grow by focusing on its core developed markets and products, both organically and by acquisition. This strategy will continue to deliver strong and consistent financial returns for shareholders

Essential Products

Value-add distribution model

Core Competencies



..... Supply chain management

Organisational Capability



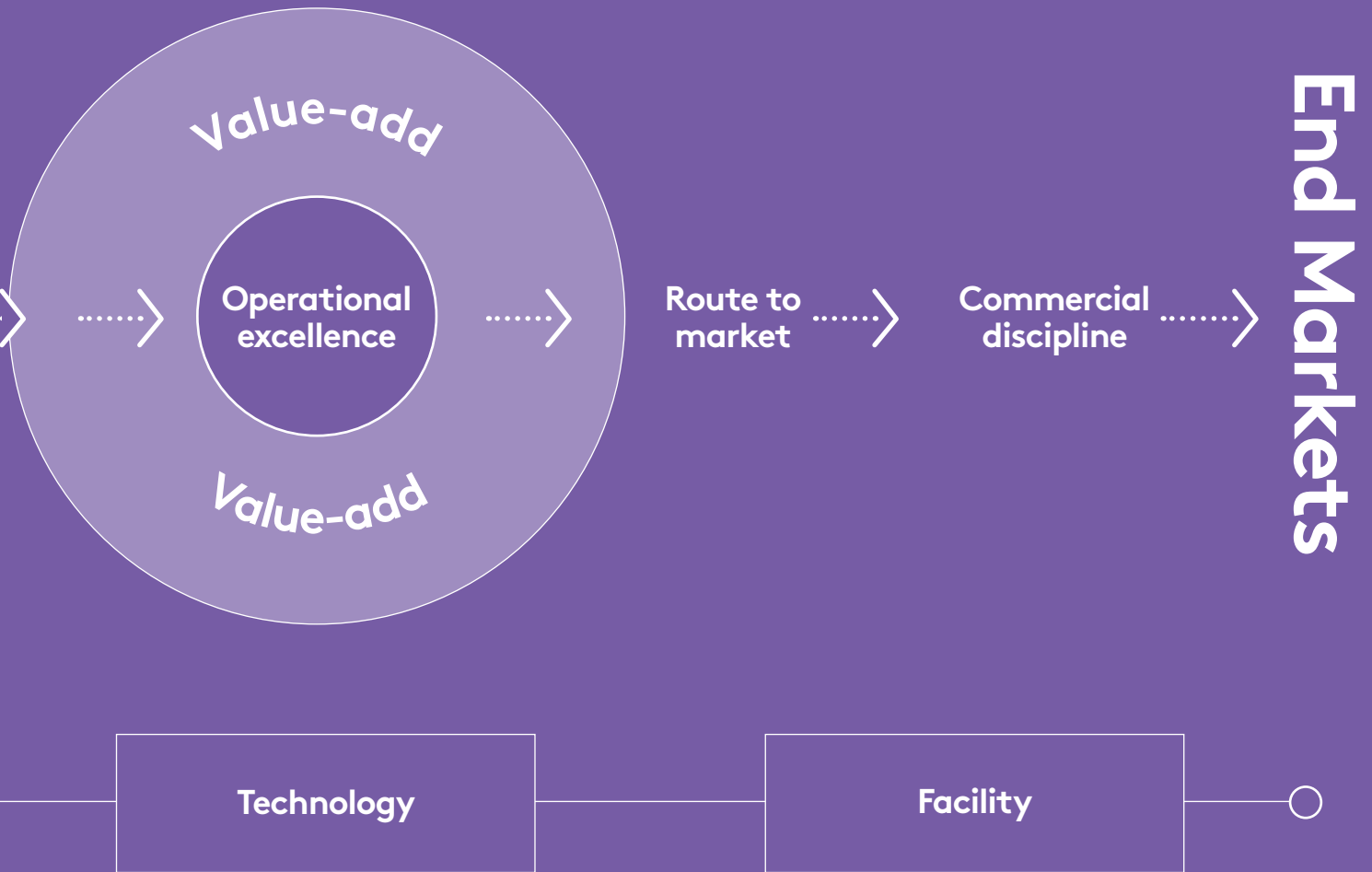


Essential Solutions



Essential Values

Diploma PLC is an international group supplying specialised products and services to a wide range of end segments in our three Sectors of Life Sciences, Seals and Controls



Financial Highlights

Year ended 30 September 2019

Strong double-digit growth in revenues and earnings

Revenue	Statutory operating profit	Statutory profit before tax
£544.7m 2018: £485.1m +12%	£84.1m 2018: £73.2m +15%	£83.5m 2018: £72.7m +15%
Adjusted operating profit¹	Adjusted operating margin	Adjusted profit before tax^{1,2}
£97.2m 2018: £84.9m +14%	17.8% 2018: 17.5% +30bps	£96.5m 2018: £84.8m +14%
Free cash flow³	Acquisition spend	ROATCE
£56.5m 2018: £60.5m	£78.3m 2018: £20.4m	22.9% 2018: 24.5%

	2019 pence		2018 pence
Adjusted earnings per share ^{1,2}	64.3	+14%	56.4
Basic earnings per share	54.7	+15%	47.5
Total dividend per share	29.0	+14%	25.5
Free cash flow per share ³	49.9	-7%	53.5

1 Before acquisition related charges and Chief Executive Officer transition costs in 2018.

2 Before fair value remeasurements.

3 Before cash payments on acquisitions and dividends.

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

Group at a Glance

Well diversified by geography and business area

We focus on supplying essential products and services across a range of specialised industry Sectors



Life Sciences

The Life Sciences Sector businesses supply a range of consumables, instrumentation and related services to the healthcare and environmental industries.

Healthcare (85% of revenue): clinical diagnostic instrumentation, consumables and services supplied to hospital pathology and life sciences laboratories for the testing of blood tissue and other samples. Surgical medical devices, consumables and services supplied to hospital operating rooms, GI/ Endoscopy suites and clinics.

Environmental (15% of revenue): environmental analysers, containment enclosures and continuous emissions monitoring systems.

Group revenue



27%

Employees

437

Primary growth drivers

- Public and private healthcare spending
- Ageing population and increasing life expectancy
- Health & Safety and Environmental regulation



Seals

The Seals Sector businesses supply a range of seals, gaskets, filters, cylinders, components and kits used in heavy mobile machinery and specialised industrial equipment.

North American Seals (61% of revenue): Aftermarket: next-day delivery of seals, sealing products and cylinder components for the repair of heavy mobile machinery.

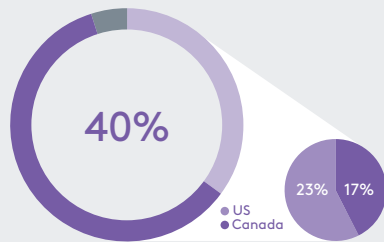
Industrial OEM: sealing products, custom-moulded and machined parts supplied to manufacturers of specialised industrial equipment.

MRO: high-quality gaskets and fluid sealing products supplied to end users with critical services in high-cost failure applications.

International Seals (39% of revenue): sealing products and filters supplied outside North America to Aftermarket and Industrial OEM customers as well as to Maintenance, Repair and Overhaul ("MRO") operations.

North American revenue (by destination) by Sector

Group revenue

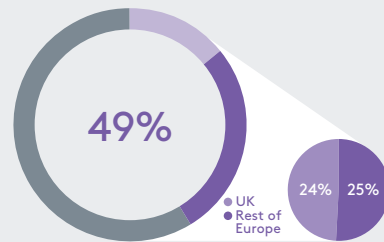


Locations

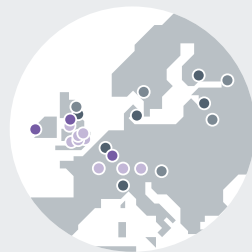


European revenue (by destination) by Sector

Group revenue

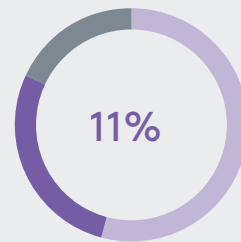


Locations



Rest of World revenue (by destination) by Sector

Group revenue



Locations



● Life Sciences
● Seals
● Controls



Controls

Group revenue



40%

Employees

1,007

Primary growth drivers

- General economic growth
- Activity and spending levels in Heavy Construction and Infrastructure
- Growth in industrial production
- Capital expansion projects at major customers

The Controls Sector businesses supply specialised wiring, cable, connectors, fasteners and control devices used in a range of technically demanding applications.

Interconnect (63% of revenue): wiring, cable, harness components and cable accessories used in specialised technical applications in Aerospace, Defence, Motorsport, Energy, Medical, Rail and Industrial.

Specialty Fasteners (21% of revenue): specialty aerospace-quality fasteners supplied to Civil Aerospace, Motorsport, Industrial and Defence markets.

Fluid Controls (16% of revenue): temperature, pressure and fluid control products used in Food & Beverage and Catering industries.

Group revenue



33%

Employees

601

Primary growth drivers

- General growth in the industrial economy
- Activity and spending levels in Aerospace, Defence, Motorsport, Energy, Medical and Rail
- Equipment installation and maintenance in Food & Beverage and Catering

Chairman's Statement

Our principal corporate objectives are to achieve double-digit growth in adjusted EPS over the business cycle; generate TSR growth in the upper quartile of the FTSE 250; and deliver progressive dividend growth targeting two times dividend cover.

Diploma has delivered another strong financial performance in 2019. The Group again achieved double-digit growth in adjusted earnings per share, generated strong free cash flow and maintained a robust balance sheet, despite having invested a record amount in acquiring new businesses this year. The results demonstrate the resilience of the Group's businesses and the consistent delivery against the Group's strategy that has allowed Diploma to build a long track record of strong financial performance and growth in shareholder value.

The Board was pleased to appoint a new Chief Executive Officer ("CEO") early in the financial year. Since joining Diploma in February this year, Johnny Thomson has demonstrated strong and effective leadership. Johnny has also completed a thorough review of the Group's strategy

which the Board has approved and which has excellent potential to create further shareholder value in the years ahead.

Shortly after the year end Nigel Lingwood, Group Finance Director, announced his decision to retire from the Board at the close of the next financial year. Nigel joined the Group in 2001 and has played a significant role in pursuing the current strategy that over the past 18 years has delivered double-digit growth in earnings and dividends. This has led to a growth in market capitalisation from £60m to over £1.9bn today. We look forward to working with Nigel during his final year with the Group, before wishing him a long and restful retirement.

Results

Group revenues increased in 2019 by 12% to £544.7m (2018: £485.1m), benefiting from both a strong 5% contribution from acquisitions and a currency tailwind of 2% from translating the results of the overseas businesses, caused by the sharp depreciation in UK sterling in the second half of the year.

After adjusting for the contribution from acquisitions completed both this year and last year, net of a small disposal last year and for the currency effects on translation, Group revenues increased by 5% on an underlying basis. The Life Sciences and Controls businesses both delivered strong underlying revenue growth of 7% and 9% respectively, but the generally weaker Industrial markets limited the more cyclical Seals businesses to 1% growth in underlying revenues.

Adjusted operating profit increased by 14% to £97.2m (2018: £84.9m) reflecting the strong growth in revenues and an increase of 30bps in adjusted operating margins to 17.8% (2018: 17.5%). Adjusted profit before tax and adjusted EPS also increased by 14% to £96.5m (2018: £84.8m) and 64.3p (2018: 56.4p), respectively.

On a statutory basis, the Group's operating profit was 15% ahead of last year at £84.1m (2018: £73.2m) after £13.1m (2018: £9.6m) of acquisition related charges, largely comprising amortisation of acquired intangible assets. Last year's statutory operating profit included one-off charges of £2.1m with respect to the previous CEO transition process. Statutory profit before tax increased by 15% to £83.5m (2018: £72.7m) and statutory EPS was 15% up on last year at 54.7p (2018: 47.5p).

The Group's free cash flow remained robust at £56.5m (2018: £60.5m); last year's free cash flow included £4.0m from the sale of a small non-core US gasket business. The outflow of cash to support working capital increased this year to £9.4m (2018: £5.1m) and was largely driven by the investment required in the US Industrial OEM business, following implementation of a new ERP system. Capital expenditure also increased this year to £10.9m (2018: £6.6m) as the investment in the new distribution facility in the US Seals Aftermarket began to ramp up and further investment was made by the Healthcare businesses in new field equipment in support of customer contracts.

Consistent and sustainable shareholder value creation

John Nicholas
Chairman





The Group has delivered strong double-digit growth in revenues and earnings¹

As indicated in last year's Annual Report, the heightened uncertainty in global industrial markets has led to a healthier pipeline of acquisition opportunities as vendors of good quality businesses decide to exit their companies, having enjoyed the benefit of relatively favourable macroeconomic conditions over the previous few years.

The Group invested a record £78.3m (2018: £20.4m) in acquisitions this year which will provide a strong contribution to operating profits in future years. The acquisition pipeline remains healthy and although acquisition processes remain competitive, the Group will retain its disciplined approach to bringing high-quality, value-enhancing businesses into the Group.

The Group's balance sheet remains robust with net debt at 30 September 2019 of £15.1m (2018: cash funds of £36.0m), after investing £78.3m in acquisitions and making distributions to shareholders of £29.8m (2018: £26.8m). The Group also has unutilised bank facilities of ca. £54m and the Group's strong balance sheet provides support to increase these facilities to finance further acquisition opportunities in the next financial year.

Dividends

The combination of strong results and free cash flow supported by a robust balance sheet has led the Board to recommend an increase in the final dividend of 15% to 20.5p per share (2018: 17.8p). Subject to shareholder approval at the Annual General Meeting ("AGM"), this dividend will be paid on 22 January 2020 to shareholders on the register at 29 November 2019.

The total dividend per share for the year will be 29.0p (2018: 25.5p), which represents a 14% increase on 2018, with the level of dividend cover remaining unchanged at 2.2 times on an adjusted EPS basis.

Governance

The appointment of a new CEO this year has provided stability in the Executive leadership of the Group. The focus this year will be on broadening the non-Executive resource to provide further support to the leadership team and to prepare for the additional corporate governance compliance requirements that come into effect for the Company in the new financial year. The Nomination and Audit Committees are now supporting the CEO in searching for a new Group Finance Director. The Remuneration Committee has updated the Remuneration Policy in light of the change in leadership and this Policy will be proposed for approval by shareholders at the AGM on 15 January 2020.

Employees

The process undertaken over the past two years in changing the leadership of the Group has been a challenging period for our employees. I would like to record my thanks to all our employees who, during this period, have remained focused on delivering excellent service and value to our customers that is the driving force behind the Group's performance and the achievement of another year of strong financial results.

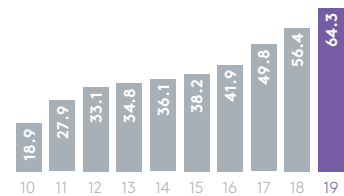
Outlook

Diploma has a strong and resilient business model with a broad geographic spread of businesses supported by a robust balance sheet and consistently strong free cash flow. This model has delivered another strong financial performance in line with our expectations.

Despite the uncertain political and economic environment impacting Industrial markets, the Board remains confident of further progress in the current financial year as moderately lower underlying growth will be offset by a strong contribution from acquisitions.

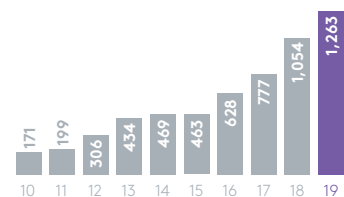
Adjusted EPS growth (pence)

+16%p.a.¹



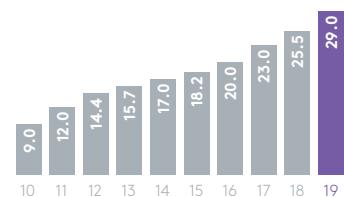
TSR growth (TSR index 2009 = 100)

+29%p.a.¹



Dividend growth (pence)

+14%p.a.¹



¹ Ten-year compound.

Chief Executive's Review

2019 has been another year of strong performance. The Group's reported revenues increased by 12%, with currency movements adding 2% and acquisitions contributing a further 5% to the revenue growth.

On an underlying basis, after adjusting for acquisitions and for currency effects on translation, Group revenues increased by 5%. Encouragingly, there was good growth in all three Sectors. Group adjusted operating margins improved by an excellent 30bps to 17.8%. As a result, the Group's adjusted earnings grew by 14% in the year. Strong cash flow generation provided funds to allow us to report a record year for acquisition spend, as well as a 15% proposed increase in the final dividend.

Sector performance

It has been a very strong year in Life Sciences. Somagen, in Canada, extended its coverage in the Canadian Provinces with its diagnostic screening product, designed to provide early detection of colorectal cancer. This product has been very well received in its market and is a great example of innovation in response to customer need. Market share gains in Vantage's Endoscopy business in Canada have also boosted growth.

The acquisition of Sphere Surgical ("Sphere") in Australia has given us a good entry point into the high-growth bariatrics segment and complements our current product portfolio in BGS. In Life Sciences, underlying revenues increased by 7%, after adjusting for currency movements and the acquisition of Sphere.

In the Seals Sector, the NA Aftermarket businesses had another strong year as we grew market share through our high-quality service offering and scale of our operation. We are currently developing a new leasehold facility in Louisville, Kentucky, which will further broaden our footprint across North America. The US Industrial OEM markets have been challenging this year. We experienced implementation issues with the ERP system earlier in the year, however with new leadership in place we are confident that these difficulties have now been resolved. VSP Technologies has made an encouraging contribution since joining the Group in July this year and extends our sealing products offering to the gasket market, supported by a high-quality, well-established customer proposition and management team. In September, we completed the acquisition of DMR Seals in the UK, which complements our existing FPE Seals business. In Seals, underlying revenues increased by 1%, after adjusting for currency movements and acquisitions.

The Controls Sector has developed well this year. The Clarendon Specialty Fasteners business had great success penetrating further into the Civil Aerospace market. The Interconnect business has been expanding successfully in Germany and has extended its business reach with the acquisition of Gremtek in France.

We continue to add new products into the Sector. Whilst market conditions in the UK have created more uncertainty in our Industrial end markets, we continue to be very positive about the future prospects for this Sector. In Controls, underlying revenues increased by 9%, after adjusting for currency effects and acquisitions.

Acquisitions

Diploma has a strong history of disciplined acquisitions. We had a very positive year for acquisitions with VSP Technologies, Gremtek, DMR Seals and Sphere all joining the Group with a total spend of ca. £78m. In the US, we have been pleased with the transition of VSP Technologies into the Group and are excited by its growth potential. VSP Technologies is a leading supplier of high-quality gasket and fluid sealing products, as well as customised solutions, to the industrial MRO market. VSP Technologies is built on strong, long-standing customer and supplier relationships supported by value-add servicing. The acquisition is consistent with our strategy and provides an exciting opportunity to extend our Seals activities in North America. In addition, three smaller bolt-on acquisitions were completed in the Seals, Controls and Life Sciences Sectors during the year – DMR Seals in the UK, Gremtek in France, and Sphere Surgical in Australia. We are very positive about the prospects for all four businesses and the strategic attributes they bring to the Group. Bolt-on acquisitions remain a key part of the Group's strategy.

Another year of strong performance

Johnny Thomson
Chief Executive Officer



Management resources

Strong management in the businesses is key to the continued success of the Group. This year we have made some important appointments to reflect our growing organisation: David Goode joined in April 2019 to lead the Controls Sector, allowing Gustav Rober to retain his focus leading our Corporate Development. In September, following the acquisition of VSP Technologies in the US, which extended the scale and opportunity of the Seals businesses, Alessandro Lala, who has been with the Group since 2006, was appointed to manage the International Seals businesses. Jill Tennant joined the Group as our first Group HR Director in May 2019. In recognition of the increasing importance of developing the Group’s talent.

In order to manage our succession and business growth requirements most effectively, while retaining our winning culture, we are committed to making internal appointments where possible. In 2019, over 50% of our senior appointments were internal candidates. The right blend of stability, internal progression and external skill is key to the strong results that will lead to our future success. Acquisition growth in 2019 has also allowed us to bring new talent into the Group.

We continue to develop the Executive Management Committee (“EMC”) which comprises the Executive Directors and Executive senior managers responsible for the major business clusters and key Group functions. The EMC meets regularly, providing the opportunity for members to broaden their perspective of the Group’s activities, reinforce the key elements of the Group’s culture and identify best practices that are transferable across the Group.

Strategy

We have a consistent strategy that is built on the strong foundations of our value-add distribution model. Since joining this year I have, together with the Executive team, reviewed and refreshed the Group’s strategy based on these strong foundations. As the Group evolves, we will continue to strengthen the Core Competencies that support that model and the Organisational Capability to execute these Core Competencies at scale. We will also focus our growth on the exciting opportunities in core developed larger markets and products. This growth will be organic and complemented as normal by acquisitions. This strategy will continue to deliver strong and consistent financial returns for shareholders.

Business Model – value-add distribution

Stable and resilient revenue growth is achieved through our focus on *Essential Products* and *Services* funded by customers’ operating model rather than capital budgets and supplied across a range of specialised industry segments. By supplying *Essential Solutions*, not just products, we build strong, long term relationships with our customers and suppliers, which support sustainable and attractive margins. Finally, we encourage an entrepreneurial culture in our businesses through our decentralised management structure. These *Essential Values* ensure that decisions are made close to the customer and that the businesses are agile and responsive to changes in the market and the competitive environment.

Business Model – value-add distribution



Strategy

Strategy

The Group has a proven and successful value-add distribution model. We hold strong positions in key niche markets with a clear route to market that provides organic growth potential and exciting acquisition opportunities in largely fragmented market environments.

Our consistent strategy will continue to evolve as the Group gets larger and more complex. However as we grow we will continue to maintain our strong foundations and to invest in and develop our Core Competencies and Organisational Capability.

It is a strategy based on continuity that builds on the foundations that underpin Diploma's success.

Strong Foundations

The Group has been built on strong foundations and our strategy will continue to build on this.

Resilient value-add distribution model

We supply Essential Products to a range of end markets. Our Essential Solutions give sustainable high margins through added-value services and customer loyalty. Our empowered management teams embody our Essential Values.

Passionate, accountable, customer-centric people

We have a decentralised structure that encourages an entrepreneurial culture across our businesses and allows our managers the freedom to run their own businesses with the support of the Group.

Strong positions in attractive markets

We hold strong positions in key local markets with potential for greater penetration in the larger developed economies and across our product portfolio.

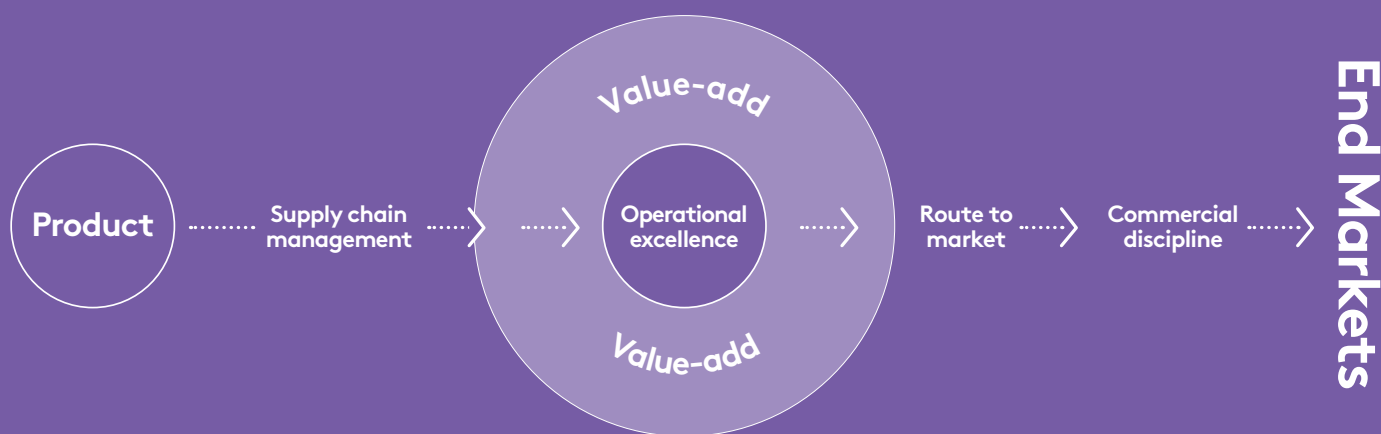
Successful M&A history

We carefully select value-enhancing acquisitions that accelerate the underlying growth and take us into related strategic markets and adjacent product opportunities.

Strong cash flow and robust balance sheet

We generate strong free cash flow and have a robust balance sheet that helps fund a disciplined acquisition strategy and provides healthy returns to shareholders.

Core Competencies



Organisational Capability



Core Competencies

Our Core Competencies help us to operationalise our proposition of Essential Products, Essential Solutions and Essential Values. As Diploma grows and becomes a broader and more complex business, we must continue to focus on and develop our Core Competencies. It is these competencies in our business model that differentiate us, protect us from disruption and deliver outstanding performance.

Supply chain management

We are a value-add distributor and our suppliers are integral to our success. Improving our demand planning and taking advantage of our increasing scale within and across our businesses will make us more competitive to our customers.

Operational excellence

Our distribution operations will become larger and more complex and we will ensure that we have the correct processes and systems in our distribution facilities that will allow us to continue to be agile and responsive to our customers' needs.

Value-add

We will continue to provide excellent service and solutions by developing our talent, our processes and our information systems that help us deliver that service and those solutions.

Route to market

We will use our scale to be more strategic in evaluating our addressable market and how we best take advantage of it. We will identify the more relevant markets, develop those markets through the right channels, invest where necessary and execute well-defined business to business sales.

Commercial discipline

Our businesses provide excellent customer service every day. Our financial model must fit our customers' financial requirements and at the same time reward our businesses fairly. Pricing remains critical to ensuring that we are always competitive to our customers and sustain our margins. This is a win-win for Diploma and our customers.

Organisational Capability

We drive our Core Competencies by investing in and developing the Organisational Capability that provides the competitive advantage across our Sectors and facilitates the improvements in our business.

Talent

We have great people and as our Group grows, we need to give our colleagues the right support, development and opportunity to grow too.

Technology

We continue to invest well in technology that will support us in delivering our Core Competencies, which is key to unlocking the operational potential in our businesses.

Facility

We are strategic about our facilities in order to improve our efficiency, quality, agility and distribution footprint.

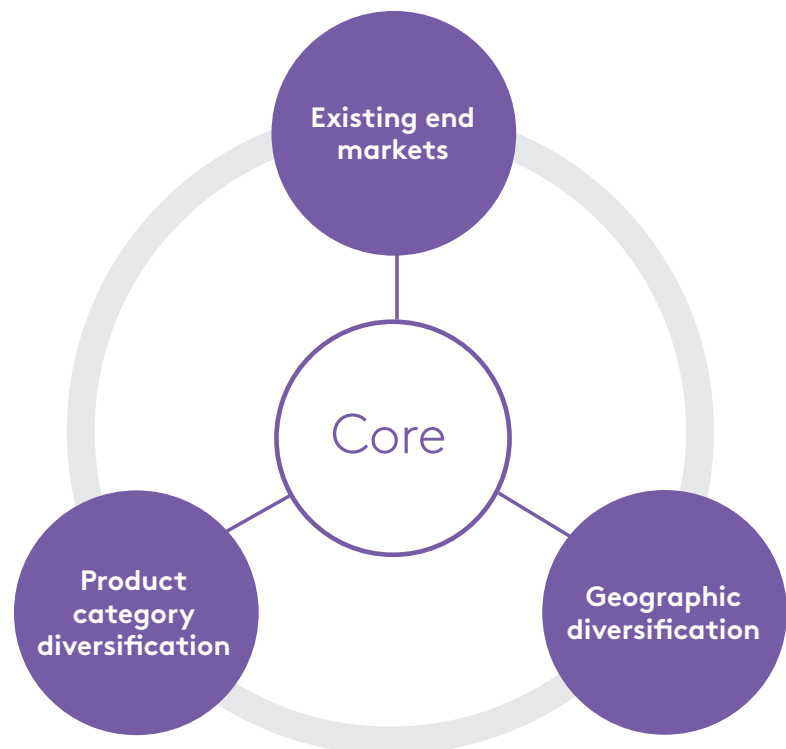
Focus the Business for Strong Growth

Diploma holds strong positions in key markets and products across each of our three Sectors. Structural market trends in our existing end markets help to sustain healthy levels of growth over the long term.

To complement this growth, encouragingly, the Group still has very low market share in its core markets and products. Those markets are also relatively fragmented. This means that we can grow by focusing on core developed markets and products, both organically and by acquisition, without being distracted elsewhere at higher risk.

The Group's increasing scale can be used selectively to support long term growth without affecting the proximity and closeness of customer relationships and services.

Small to medium sized bolt-on acquisitions continue to play an important part in the development of our Group. In a fragmented market, there are many high-quality operators, and the Group has a healthy balance sheet to reinvest. This year has been a record year with four new businesses joining the Group. We will continue to pursue similar businesses that have the right strategic fit and meet our criteria.



Strategic Priorities and KPIs

Consistent and sustainable shareholder value creation

Diploma has delivered excellent shareholder returns over many years and the Group's businesses have significant potential to continue this track record.

The key performance indicators ("KPIs") we use to measure the success of the business model relate to recurring income and stable underlying revenue growth, sustainable and attractive margins and organisational health. This year, underlying revenue growth, after adjusting for currency movements and acquisitions, has been a robust 5%, with the growth rate softening in the second half of the year. Reported growth has been 12% in the current year and on a five-year CAGR basis.

The agility and responsiveness of the organisation is more difficult to measure directly, but non-financial KPIs can give an indication of the organisational health. The number of working days lost to sickness has consistently been only ca. 1.4% a year and over the last five years, the average length of service for all employees has been ca. 6.7 years (ca. 10 years for the senior management cadre).

Acquisitions are not made just to add revenue and profit, but rather to bring into the Group successful businesses that add value to the Group from their growth potential, capable management and a good track record of profitable growth and cash generation. As part of our strategy to focus the business for strong growth, we invest in the businesses post-acquisition to build a firm foundation to allow them to move to a new level of growth and improve operating margins. These acquisitions form a critical part of our Sector growth strategies and are designed to generate a pre-tax return on investment of at least 20% and hence support our Group objectives for return on total investment.

Again we measure the success of the growth of the business with KPIs, the first of which is acquisition spend. As part of the Group's objective of strong double-digit growth we have an acquisition capacity of up to two times net debt/EBITDA, though year-on-year spend will vary with the acquisition environment. This year, the Group invested ca. £78m in acquisitions, bringing the total over five years to ca. £190m. The acquisitions completed over the last five years have contributed ca. 25% of 2019 revenues.

The Group's return on total investment measure is the pre-tax return on adjusted trading capital employed, excluding net cash, but including all goodwill and acquired intangible assets ("ROATCE"). This is used to measure the overall performance of the Group and very importantly, our success in creating value for shareholders through our acquisition programme. Over the last five years, ROATCE has exceeded the 20% target and this year was 23%.

As the Group continues to grow it will continue to pursue these metrics in its financial model.

Financial model

Revenue growth

10%+

Adjusted operating margin

17%+

Free cash flow conversion

ca. 90%+

Net debt/EBITDA

<2x

Dividend cover

2x adjusted EPS

Return on adjusted trading capital employed

20%+

Key Performance Indicators

Initiatives

Key performance indicators

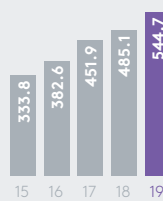
GDP+ underlying revenue growth

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

Revenue growth (£m)

+12%

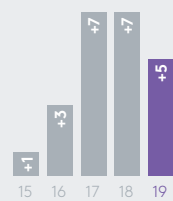
Five-year compound



Underlying revenue growth (%)

+5%

Five-year average



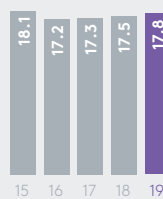
Attractive margins

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

Adjusted operating margin (%)

17.6%

Five-year average



Adjusted operating margin (bps)

+200–300bps

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

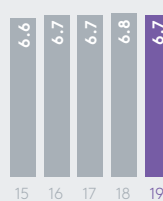
Agile and responsive organisation

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

Length of service (years)

6.7 years

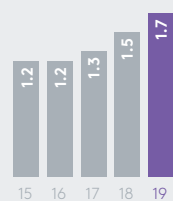
Five-year average



Average working days lost to sickness

1.4%

Five-year average



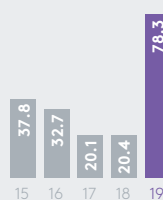
Acquisitions to accelerate growth

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

Acquisition spend (£m)

£37.9m

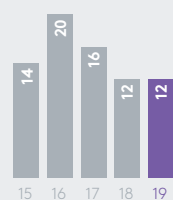
Five-year average



Revenue from acquisitions (% of total)

15%

Five-year average



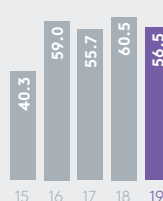
Strong cash flow

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

Free cash flow (£m)

£54.4m

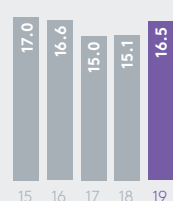
Five-year average



Working capital (% of revenue)

16%

Five-year average



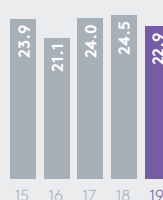
Value creation

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

ROATCE (%)

23%

Five-year average



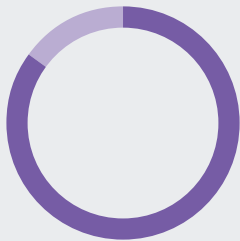


Life Sciences

The Life Sciences Sector businesses supply a range of consumables, instrumentation and related services to the healthcare and environmental industries

Principal segments

- 85% Healthcare
- 15% Environmental



Geography

52%

Canada

23%

Australasia

25%

Europe

Customers

84%

Clinical

2%

Life Sciences Research

9%

Utilities

1%

Other Life Sciences

4%

Chemical & Pharmaceutical

Products

69%

Consumables

9%

Service

22%

Instrumentation

Healthcare

The Diploma Healthcare Group ("DHG") operates in three principal geographies – Canada, Australasia and Europe. In Canada, DHG supplies to the ca. 600 public hospitals across the country as well as to private clinics and pathology laboratories. Somagen Diagnostics ("Somagen") serves the In-vitro Diagnostics ("IVD") market supplying a range of consumables and instruments used in cancer diagnostics, specialty diagnostics and infectious disease segments of the market. It is a leading supplier to the growing cancer screening and the companion diagnostics markets. AMT/Vantage comprises the AMT Surgical ("AMT") and Vantage Endoscopy ("Vantage") divisions. AMT supplies equipment, specialised instrument sets, rigid and flexible surgical endoscopes and consumables for diverse surgical applications in hospital operating rooms. Vantage supplies endoscopes and related consumables, therapeutic devices and services to GI Endoscopy suites in hospitals and private clinics providing out-patient diagnostic and therapeutic procedures.

In Australia and New Zealand, DHG also supplies to hospitals, private clinics and pathology laboratories. Abacus dx is a leading supplier of instrumentation and consumables to the Pathology (IVD), Scientific Research and Medical Simulation segments of both public and private markets. Big Green Surgical ("BGS") supplies both the Australia and New Zealand specialty surgical markets with specialised equipment and consumables used across diverse applications in hospital operating rooms. DHG expanded BGS's specialty surgical focus with the acquisition of Sphere Surgical in Australia in September 2019 which broadened the product range into the bariatric surgery segment. Both Abacus dx and BGS share several common market leading suppliers with DHG's Canadian businesses.

In Europe, DHG operates through Techno-Path (Distribution) Limited ("TPD"), an established supplier of leading edge technologies to the Biotechnology and Healthcare markets in Ireland and the UK. Similar to the other DHG businesses, TPD focuses on specialised laboratory diagnostics (IVD) and specialty medical device segments, again leveraging several common

suppliers with DHG's Canadian and Australian businesses. Unique to the TPD business, is an expanded focus on its Biotechnology division. The Biotechnology division includes detection, testing and monitoring solutions across numerous sectors of the market including: agrifood & beverage, dairy, water testing, pharmaceuticals and research and development.

Environmental

The a1-group is a supplier to Environmental testing laboratories and to Health & Safety engineers. The a1-envirosciences business is based in Germany, with operations in the UK, Netherlands and France. The business has two divisions, a1-safetech and a1-envirotech and is a specialist supplier of containment solutions and analysers for chemical, petrochemical, environmental, research and pharmaceutical technology.

The a1-CBISS business, based in the UK, supplies equipment, bespoke engineering, installation and service support for continuous emissions monitoring systems ("CEMS"), as well as a range of gas detection and personal protection devices.

Market drivers

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

The Canada Health Act (the "Act") ensures universal coverage for all insured persons for all medically necessary services provided by hospitals, physicians and other Healthcare providers. Another key demand driver in Canada, as well as in DHG's other geographic markets, is the growing ageing population and the expectation for longer, healthier lifestyles and the corresponding necessity for new technology and improved service delivery.

Principal operations

Healthcare

Somagen Diagnostics	Edmonton, AB, Canada
AMT/Vantage	Kitchener, ON, Canada
Abacus dx	Brisbane, QLD & Melbourne, VIC, Australia; Auckland, New Zealand

Big Green Surgical/ Sphere Surgical	Melbourne, VIC, Australia
Techno-Path (Distribution) Limited	Ballina, Co. Tipperary, Ireland

Environmental

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

The Canadian Provinces are responsible for the delivery of Healthcare services, but the Federal Government partially controls delivery through Federal Provincial transfer payments, which represent the largest source of revenues for the Provinces. The relative stability and consistency in funding to each of the Provinces, guaranteed through the Act, ensures that the market remains well funded through the economic cycle and current expenditure of 10.7% of GDP, C\$6.5k per capita, places Canada as the seventh largest healthcare spender as a percentage of GDP in the OECD countries.

Over many years, Healthcare expenditure has grown steadily with annual variations mostly dependent on the periodic additional tranches of funding provided by individual Provinces. In periods when the economy has been slower, Healthcare funding has still shown growth, albeit at reduced levels. In 2018, public Healthcare spending in Canada was ca. C\$186bn, with the largest category of expenditure represented by the hospital sector at ca. 35% of spending.

The Healthcare market in Australia shares with Canada many of the same attractive characteristics for specialised distribution. While privately funded Healthcare is more prevalent in areas such as surgery and laboratory testing, public sector Healthcare funding is still large and supported by a stable, resource based economy. In 2018, Australian health expenditure was A\$186bn, of which ca. 68% was publicly funded by a combination of Federal, State and Territory governments. As with Canada, Australia has a large geography to be covered, low population density and purchasing processes that vary by State. These characteristics necessarily demand a significant investment by manufacturers in commercial, technical and service resources, which makes the specialised local distribution model a very attractive mechanism for manufacturers to serve the local markets.

In recent years, the Canadian and Australian economies have come under pressure from lower oil prices and reduced demand for the countries' natural resources. This tougher economic environment resulted in greater pressure on budgets throughout the Healthcare systems in both countries. This has led to tighter constraints on Healthcare funding through targeted controls imposed on the number of laboratory tests and surgical procedures as well as regional consolidation of testing and service provision. It has also contributed to more rigorous tendering processes overseen by large consolidated Group Procurement Organisations ("GPOs") for expenditure on capital equipment and consumable supplies. Even with such pressures, however, Healthcare funding has shown positive growth in total Healthcare expenditure.

The principal market driver for the TPD business, similar to Canada and Australasia, is Healthcare funding in the UK (NHS) and Ireland (HSE), which totals ca. £226bn, representing ca. 10% of combined GDP. The UK accounts for ca. 90% of the total funding and ca. 80% is provided by public funding. 2017/18 estimates reflect an acceleration in Healthcare expenditure annual growth in both the UK and Ireland at 4.5% and 6.4% respectively, compared with 2013/18 Healthcare expenditure CAGR of ca. 3%.

The a1-group supplies to customers in the **Environmental** industry in the UK, Germany and France. The market demand is largely driven by Environmental and Health & Safety regulations and growth in recent years has been driven by the need to be compliant with a range of EU regulations. Since market demand is driven by regulation, this ensures reasonably steady demand for essential consumable products and services, though customers may defer capital expenditure during significant downturns in the economy.

Canadian Healthcare expenditure (C\$bn)

			% growth
19	186.3	78.1	3.9%
18	179.5	75.0	3.9%
17	172.0	72.9	3.6%
16	165.6	70.8	3.9%
15	161.5	66.1	4.5%

■ Public ■ Private

Source: Canadian Institute for Health Information. Includes capital expenditure, forecast data 2018 and 2019.

Australian Healthcare expenditure (A\$bn)

			% growth
18	126.7	58.8	2.9%
17	124.2	56.0	5.7%
16	114.7	55.9	5.5%
15	108.1	53.5	4.5%
14	104.9	49.8	5.3%

■ Public ■ Private

Source: Australian Institute of Health & Welfare. Includes capital expenditure.

UK Healthcare expenditure (£bn)

			% growth
17	138.7	32.5	3.4%
16	135.6	30.0	5.0%
15	129.5	28.2	3.3%
14	125.6	27.0	5.0%
13	119.5	25.9	3.6%

■ Public ■ Private

Source: UK Health Accounts (2018 data not available). Excludes capital expenditure.

Total current Healthcare expenditure as a percentage of GDP

	2014	2015	2016	2017	2018
Canada	10.1%	10.6%	10.8%	10.7%	10.7%
Australia	9.0%	9.3%	9.2%	9.2%	9.3%
Ireland	9.7%	7.3%	7.4%	7.2%	7.1%
UK	9.8%	9.7%	9.7%	9.6%	9.8%

Source: OECD, forecast data 2018

Total current Healthcare expenditure per capita

	2014	2015	2016	2017	2018
Canada (C\$000)	5.7	5.9	6.1	6.2	6.4
Australia (A\$000)	6.3	6.5	6.7	6.9	7.2
Ireland (€000)	4.0	4.1	4.2	4.4	4.7
UK (£000)	2.8	2.8	2.9	3.0	3.1

Source: OECD, forecast data 2018

Life Sciences continued

Highlights

- Sector revenue growth of 8%; underlying growth of 7% after adjusting for currency effects and a small surgical acquisition in Australia completed late in the year
- In Canada, DHG underlying revenues increased by 10% with strong consumable and capital revenues from its market-leading new technology products, extending its cancer diagnostics programme in Somagen and endoscopy product lines in Vantage
- In Australia and New Zealand, underlying revenues increased by 8%. Abacus dx reported strong growth across its portfolio of products. Diploma acquired Sphere Surgical in September, adding bariatrics to the product portfolio of the BGS surgical products business
- TPD underlying revenues declined 7% in Ireland as the business rebuilds its product portfolio and restructures its commercial divisions
- The Environmental businesses reported 9% underlying revenue growth with strong revenue growth in the a1-CBISS business, following a good recovery in the second half for CEMS installations and associated services

Sector performance

Reported revenues of the Life Sciences Sector businesses increased by 8% to £145.8m (2018: £134.7m) with strong revenue growth from both the DHG and a1-group. Revenues benefited from a currency tailwind of 1% on translation of the results from the overseas businesses to UK sterling. After adjusting for currency effects and the acquisition of Sphere Surgical, underlying revenues increased by 7%.

Adjusted operating margins grew by 120bps to 18.9% largely reflecting strong operating cost leverage across both the DHG and Environmental businesses. Gross margins were slightly weaker reflecting the impact of transactional currency pressures on the Healthcare margins, but favourable currency hedges helped offset some volatility of the Canadian and Australian dollars relative to the US dollar and Euro during the second half of the year. Adjusted operating profits increased by 15% to £27.5m (2018: £23.9m).

The Life Sciences businesses invested £3.3m (2018: £3.5m) in new capital during the year of which £2.7m (2018: £2.3m) was spent on acquiring field equipment for both new placements in hospitals and laboratories and for loan equipment and demonstration models to support existing placements. The increased spend on field equipment was largely driven by the launch this year of a new series of flexible endoscopes, and expansion and conversion of special biochemistry technology in Australasia, together with the replacement of smoke evacuation products to extend contracted business. The balance of £0.6m was split between furnishings for the newly renovated AMT/Vantage facility and service equipment improvements and upgrades.

The IT infrastructure across the Healthcare businesses was also upgraded. Free cash flow increased strongly to £23.2m (2018: £17.3m), largely reflecting strong operating cash flow, which also benefited from a cash inflow from reduced working capital.

Healthcare

The DHG businesses, which account for 85% of Life Sciences revenues, increased underlying revenues by 7% after adjusting for currency effects and the small acquisition.

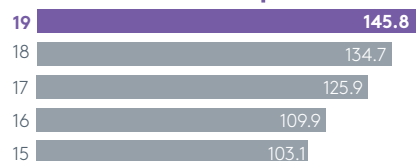
In Canada, underlying revenues increased by 10% driven by new technologies in all businesses, despite the ongoing backdrop of regional consolidation of GPOs. The GPOs continue to restructure and amalgamate, leading to harmonised contracting, and rationalised service provision in the laboratory sector in Quebec, in particular. In response the DHG businesses continue to seek new suppliers that develop and provide innovative products to the market.

Somagen's core Clinical Diagnostics business delivered an underlying increase of 10% in revenues, with sustained growth in consumable and service revenues. Capital sales decreased reflecting the impact of laboratory centralisation, particularly in Quebec. Demand for diagnostic testing, both cancer screening and companion diagnostics, remained robust. Somagen implemented two new large Provincial contracts to provide colorectal cancer screening products and services with the stability of long term contracts. Somagen continued to pursue new supplier recruitment programmes, resulting in new targets entering the contracting phase across the Specialty Diagnostics, Microbiology and Molecular Diagnostics segments of the market.

Revenue (£m)

(compound growth over five years)

+10% p.a.



Revenue

£145.8m

	2019	2018	
Revenue	£145.8m	£134.7m	+8%
Adjusted operating profit	£27.5m	£23.9m	+15%
Adjusted operating margin	18.9%	17.7%	+120bps
Free cash flow	£23.2m	£17.3m	+34%
ROATCE	22.0%	19.1%	+290bps

AMT/Vantage, the combined Surgical and Endoscopy businesses in Canada, delivered strong underlying growth of 10% in revenues, particularly driven by Vantage's continued success with the introduction of a new series of gastric endoscopes. The new technology in these endoscopes has successfully driven current customer contract extensions as well as new contracted business. Continued diversification across both Vantage's endoscopy division and AMT's surgical speciality division offers growth in new segments of the market as well as offsetting some of the maturing, traditional electrosurgical market. AMT/Vantage's discipline around portfolio life cycle management, has yielded new suppliers that will drive future growth in both the GI/Endoscopy and Specialty Surgical segments of the Canadian market.

In Australasia, Abacus dx delivered 11% underlying growth in revenues driven by expansion of product offerings in the immunology market and conversion of special biochemistry technology. However, revenues were also impacted by the continuing consolidation of testing within the Australian Clinical Diagnostics market and broader based GPOs in the fragmented diagnostics market. BGS, the Surgical Products business in Australasia, stabilised revenues with a modest 1% underlying growth after the loss of a key surgical supplier last year. The acquisition of Sphere Surgical provided access to the Bariatric Surgery market, a new segment for BGS. BGS also made good progress in securing new specialty surgical suppliers that will drive further growth.

The TPD business in Ireland and the UK reported declining underlying revenues of 7% attributed to its Medical and Surgical business in Ireland as it continues to manage the transition of a number of medical and surgical suppliers who have moved from specialised distribution to a direct supply model. The Biotech business grew 13% on an underlying basis, with the Clinical business remaining largely unchanged on prior year. The business has restructured into two commercial divisions, Medical Science and Clinical Science, with Medical Science aligning to the Medical and Surgical markets, and Clinical Science aligning to the IVD and Biotech markets. Both divisions have focused on portfolio development efforts resulting in new suppliers that will provide new growth in the future.

Environmental

The a1-group of Environmental businesses in Europe, which account for 15% of Life Sciences revenues, saw underlying revenues increase by 9%, with both businesses performing strongly in the second half of the year.

The a1-envirosciences business, based in Germany, increased underlying revenues by 4% driven by expanding demand across Europe for elemental analysers and the associated service contracts. The increasing environmental awareness and in particular, the anticipated regulations on toxic polyfluorinated compounds, found in a range of manufactured products, is creating continued demand for these analysers in R&D and Environmental control. Health & Safety regulations also continue to increase demand for customised containment enclosures for the safe weighing of hazardous materials. The business has invested in additional service personnel and an IT based field service management system to support the larger installed base and capitalise on the demand from customers for faster response times.

The a1-CBISS business based in the UK delivered strong underlying growth of 15% in revenues against a weak prior year comparator. Revenue growth reflected a strong recovery in order placement for CEMS and associated service, as well as growth in the gas detection product segment. With strong CEMS capital sales, the associated service contracts provide for future revenue growth.

Potential for growth

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

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

Pursue further Healthcare acquisition opportunities in Northern Europe, particularly Nordics

Build scale through pursuing further Healthcare acquisition opportunities in Ireland/UK

Continue to develop product portfolio and geographic reach of Environmental businesses

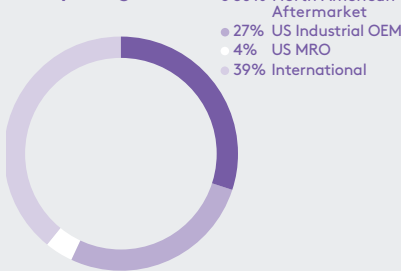
Optimisation of IT infrastructure across Canada and Australasia businesses to improve operational efficiency



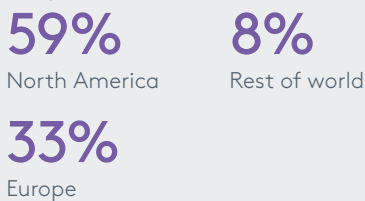
Seals

The Seals Sector businesses supply a range of seals, gaskets, filters, cylinders, components and kits used in heavy mobile machinery and specialised industrial equipment

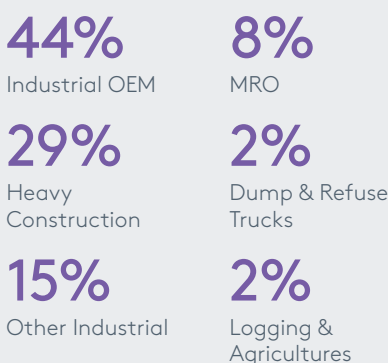
Principal segments



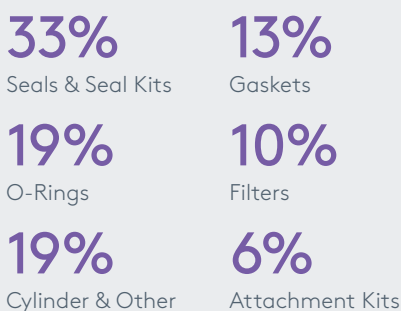
Geography



Customers



Products



North America

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

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

In Maintenance, Repair and Overhaul ("**MRO**") operations, VSP Technologies supplies high quality gaskets and fluid sealing products to end users with critical services in high cost of failure applications. The business works directly with customer engineering and maintenance operations to improve sealing performance providing flanged connection expertise, product recommendations and installation training to best practices. Market focus is Transportation (Rail and ISO Tanks), Chemical Processing, Power (Generating and LNG facilities), Marine (US Navy and Coast Guard) along with Food & Beverage. Products are delivered or shipped from six strategic locations from Virginia to Texas. Customer product availability requirements range from hours to days.

International

The International Seals businesses outside NA supply a range of seals, gaskets, filters, custom moulded and machined parts and hydraulic cylinder components to both Aftermarket and Industrial OEM customers.

The businesses also supply products to end users operating process plants within the Mining, Oil & Gas, Pharmaceutical, Chemical, Food & Beverage and Energy sectors, where products are required to support MRO operations.

Market drivers – North America

In the NA **Aftermarket** businesses, the principal drivers are GDP growth, construction spending, and sales of new construction equipment. In 2019, the US economy is forecast to show annual GDP growth of 2.3% (2018: 2.9%). Retail sales and consumer spending continue to be positive, but the ongoing trade dispute with China reduced business investment and slower job creation has reduced GDP growth. However, construction spending remains at, or near, record highs and is forecast to increase by 4% in 2019. The construction industry remains strong even though shortages in skilled labour and rising material costs persist.

New construction equipment sales peaked in 2017/18, which had an adverse effect on repair sales in the first half of the fiscal year as the equipment was still under original warranty (this trend reversed late in the second half). Increased rental fleet utilisation resulted from limited availability of new machines in the first half. The net effect of sluggish machine sales (due to limited inventory) and increased rental utilisation were fewer opportunities for HKX to kit new machines. Demand in 2019 and forward, levelled out to historical growth levels of ca. 5%.

Canada's economy was relatively strong through the first half of 2019, growing nearly 4% in the second quarter. Most of this growth was due to one-time factors, however, such as the easing of restrictions on domestic oil production. The economy is facing strengthening headwinds in the form of continued trade uncertainty, highly indebted households and contracting consumer demands. Major banks have revised their forecast growth from 2.1% to 1.5% in 2019 and 1.6% in 2020.

In general, the economic conditions in the South and Central American economies served by the NA Aftermarket businesses

Principal operations

North America

Aftermarket

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

Industrial OEM

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

MRO

VSP Technologies	Richmond, VA, Houston, TX, Parkersburg, WV, Kingsport, TN, Baton Rouge & Lake Charles, LA, US
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International

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

continue to be challenging due to local and global uncertainty with small improvements expected due to domestic demand.

For the US **Industrial OEM** Seals businesses, a downturn in the US Industrial Production Index during the second half of the year provided headwinds to the growth experienced in previous years. This index is consistent with the Manufacturers' Purchasing Managers Index, which was declining for most of 2019 as NA and Global manufacturing faced uncertainty from the US-China trade discussions.

In **MRO**, VSP Technologies has operations throughout the Southern United States and is a leading supplier of high-quality gaskets and fluid sealing products, as well as customised solutions, to the industrial MRO market. The business's core customers are those processing and transporting hazardous and corrosive materials, along with those in other industrial markets, including power generation, pulp, paper and marine. The principal market driver is US Industrial Production and in particular the subset relating to Chemical manufacturing and the Chemical Activity Barometer. Although the US Industrial Production weakened in the second half of 2019, the baseline demand for fluid sealing in critical services at fixed plant locations is typically resilient to market cycles, but growth can be tied to capital expansion projects at major customers. Power Generation continues to face headwinds as gas replaces coal as a fuel source in the US, although VSP Technologies provides opportunities to target OEM turbine manufacturers and LNG facilities.

Market drivers – International

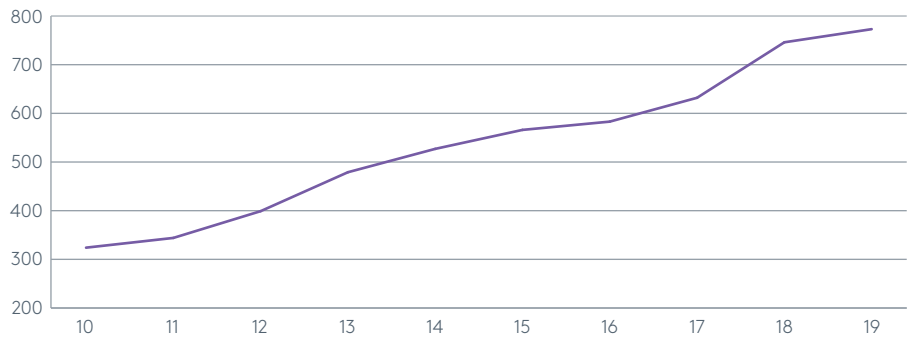
The International Seals businesses operate in a range of countries and diverse market sectors and each has its own specific market drivers. The most relevant market drivers and indicators are therefore the general GDP growth and Industrial sector performance for the major geographies in which the businesses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

In the UK, economic growth is forecast to be lower in 2019 at the modest level of ca. 1.2% (2018: 1.6%), with Brexit-related uncertainties holding back investment. The UK Construction sector, which drives the Aftermarket business, has been stuck in a downturn since the beginning of 2019 reflecting the impact from caution among customers, heightened Brexit uncertainty and a weak outlook for the UK economy.

Nordic economies have been resilient over the last three years, with continued GDP growth supported by strong export demand in Denmark and Sweden and stable oil prices supporting demand in Norway. In 2019, average growth across the region is forecast to decrease to ca. 1.7% (2018: 1.8%) impacted by global trade uncertainties.

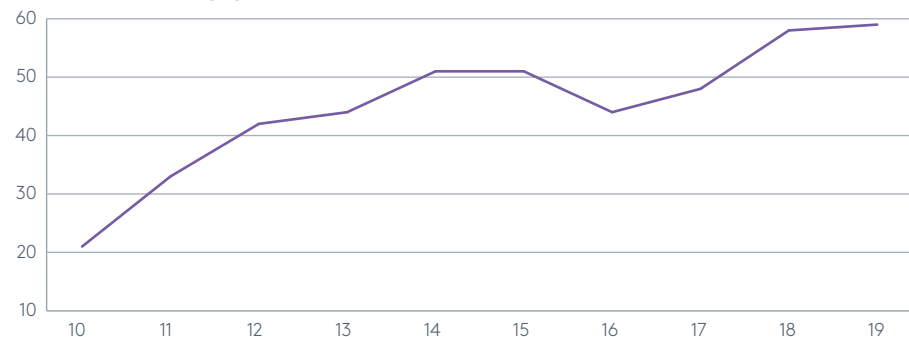
In Switzerland, after strong growth in 2018 as exporters benefited from the depreciation of the Swiss franc against the Euro, GDP growth is forecast to decrease to ca. 1.1% in 2019 (2018: 2.3%). The strengthening of the Swiss franc against the Euro through the second half of 2018 into 2019 combined

US construction spend (US\$bn)



Source: Cyclast Intercast, 2019 estimate.

US construction equipment units (000)



Source: Cyclast Intercast, 2019 estimate.

US industrial production index



Source: US Federal Reserve (seasonally adjusted).

GDP growth in principal International Seals territories

Real GDP growth	2015	2016	2017	2018	2019
UK	+2.3%	+1.9%	+1.8%	+1.6%	+1.2%
Nordic region	+2.5%	+2.3%	+2.3%	+1.8%	+1.7%
Switzerland	+1.2%	+1.4%	+1.1%	+2.3%	+1.1%
Russia	-2.5%	-0.2%	+1.6%	+1.7%	+1.6%
Australia	+2.5%	+2.6%	+2.3%	+3.0%	+2.1%

Source: IMF and Nordic Statistics

with the global trade uncertainties have reduced the 2019 growth forecasts.

In Russia, US and EU sanctions continue to hinder economic activity. However, the economy is benefiting from a stabilisation of oil prices and foreign exchange rates and lower levels of inflation and, after having contracted by 2.5% in 2015, GDP grew by 1.7% in 2018 with further growth of 1.6% forecast in 2019.

In Australia, the decline in mining investment following the downturn in the Mining sector is set to flatten, with increased non-mining business investment and government spending supporting growth. In 2019, despite slowing global demand and a cooling housing market, GDP growth should continue at a steady pace of 2.1% which represents a moderation from 3.0% in 2018.

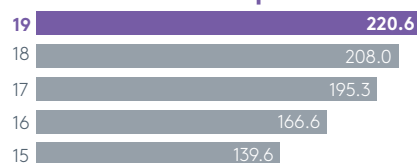
Seals continued

Highlights for the year

- Sector revenue growth of 6%, reflecting contribution from acquisition of VSP Technologies; underlying growth of 1% after adjusting for currency and acquisitions
- NA Aftermarket underlying revenues increased by 2%, driven by improved trading conditions in the second half of the year as large mobile machinery continued to move out of warranty period; HKX revenues declined marginally reflecting a reduced supply of new equipment
- US Industrial OEM revenues significantly impacted this year by combination of softening US Industrial markets and operational issues arising on implementation of new ERP; underlying revenues decreased by 6% on prior year. ERP issues now resolved and new leadership team appointed at end of year
- VSP Technologies acquired in July has made solid contribution in line with expectations
- International Seals reported an increase in underlying revenues of 4%; weaker second half reflecting softer European industrial markets

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

+13% p.a.



Revenue

£220.6m

Sector performance

Reported revenues of the Seals Sector businesses increased by 6% to £220.6m (2018: £208.0) with the acquisitions in the second half of the year of VSP Technologies and DMR Seals contributing £9.3m to Sector revenues. Underlying revenues increased by 1%, after adjusting for these acquisitions, net of a small disposal last year and for currency effects on translation of results to UK sterling.

Adjusted operating margins remained unchanged at 17.3% with stronger gross margins, particularly in the NA Aftermarket business following robust price increases and strong freight recoveries. However, these margins were largely offset by investment in the US Industrial OEM business necessary to resolve issues that arose on implementation of a new ERP system. The International Seals businesses reported adjusted operating margins marginally below the prior year, reflecting the impact of softer demand in their key markets.

The Sector invested £5.1m (2018: £2.0m) in capital expenditure during the year reflecting the ramp up of investment of £3.2m in a second distribution facility for the NA Aftermarket business and a further £0.6m (2018: £0.8m) was invested in completing the implementation of the new ERP system in the US Industrial OEM business. The International Seals businesses invested £1.0m on beginning an implementation project for new ERP systems in both Kubo and in FPE Seals and on new warehouse machinery.

Free cash flow was significantly impacted by difficulties that arose from the ERP implementation this year in the US Industrial OEM business and decreased by £8.2m to £17.7m (2018: £25.9m). These difficulties were exacerbated by the expansion of trade tariffs in the US during the year. Both issues contributed to a substantial increase in inventories in this business necessary to help customers mitigate the impact of tariffs, manage increased lead times from select suppliers and increased on-hand stock requirements to maintain service levels to customers.

North American Seals

The NA Seals businesses, which accounts for ca. 61% of Seals revenues, reported revenues up 7% on the prior year which included a strong contribution from VSP Technologies, acquired in July 2019. Underlying revenues decreased by 1%, after adjusting for this acquisition, net of a small non-core disposal last year and the weakening of UK sterling against both the US and Canadian dollar.

The US **Aftermarket** businesses increased revenues by 2% on an underlying basis, driven by improved trading in the second half of the

year in the Repair market, after a weak first half caused by an unusually high influx of new heavy mobile equipment in the past few years, which remained under the original manufacturer's warranty. The Aftermarket business is now beginning to benefit as this new equipment moves out of warranty. HKX also experienced slightly softer markets from a reduced supply of new mobile equipment in the dealer network and competition from excavator OEM manufacturers.

In the domestic Aftermarket, Hercules reported underlying revenues up 3% on the prior year with the Repair and Distributor segments continuing to provide growth and opportunities. Smaller seal distributors continued to purchase from Hercules to avoid seal manufacturer lead times and minimum order quantities. Hercules also added new products to its portfolio as well as broadening both the scope of customers and equipment supported. After several years of product development, Hercules are now making successful inroads to supply seals into the heavy mobile equipment Rental sector, including namely Aerial Lifts, Skidsteer Loaders and Front-end Loaders. New market opportunities include seal kitting services for industrial plants of OEMs and industrial MRO. E-commerce continued to deliver strong year-on-year growth and now accounts for 34% of invoices processed and 28% of Hercules US revenues. A new version of the e-commerce site has been developed during the year and will be rolled out in early 2020. This will provide greater functionality, faster response and greatly enhanced search engine optimisation.

The US\$10m project to develop a second distribution facility made strong progress during the year, with new logistic equipment being installed in a new 120,000 sq ft leased facility in Louisville, Kentucky. During the year ca. £0.2m of one-off costs were incurred on this project; further one-off/dual running costs of ca. £2m will be incurred in the next financial year, prior to completion of the project in late 2020. When fully operational, this facility will comprise highly technical warehouse automation that will allow much greater access to expanded territories in the US, as well as more competitive shipping logistics.

In Canada, revenues increased by 6% in local currency terms. This outpaces a Canadian economy that has seen some volatility over the past year, with market share being gained from both Repair and Industrial OEM customers. During the year, Canada also successfully leveraged the Hercules e-commerce platform, which now accounts for 9% of invoices and 5% of Canadian revenue.

	2019	2018	
Revenue	£220.6m	£208.0m	+6%
Adjusted operating profit	£38.1m	£36.0m	+6%
Adjusted operating margin	17.3%	17.3%	-
Free cash flow	£17.7m	£25.9m	(32%)
ROATCE	19.3%	25.3%	(600bps)

In markets outside of NA, Hercules faced headwinds because of the impact of increased tariffs that led to a reduction in cylinders manufactured in China and delivered to export markets. Despite this reduction in cylinders, moderate revenue growth of 2% was reported in Central and South America.

HKX revenues declined by 3% as the business faced significant equipment shortages which reduced HKX kitting opportunities as excavator OEM manufacturers enhanced both their capability and availability of factory installed auxiliary hydraulics. The introduction of mandated Tier 4 mobile equipment in Canada from 1 January 2019 also contributed to weaker demand, after a strong finish for Tier 3 machines last year.

The US **Industrial OEM** business was disrupted significantly this year by the difficulties that arose on implementation of the new ERP system on 1 October 2018 and underlying revenues were 6% below the prior year. Revenues also suffered from a softening US industrial market in the second half of the year, caused by the disruption from increased trade tariffs and weaker global economies leading to a decline in US exports. With this background, larger customers in particular continued to seek pricing concessions in exchange for both retaining and gaining additional business. In response, management has also secured price reductions from its suppliers and has taken advantage of suppliers who relocated production facilities outside of tariffed regions, to maintain competitiveness in the marketplace.

The business has a number of large key accounts across a range of specialised industrial applications in industries including Water, Medical, Oil & Gas, Fluid Handling and Food Equipment, as well as Consumer Products. Despite the operational difficulties, Water, Medical and Consumer Products continued to show positive gains as new projects and products were introduced. However the business saw a decline in revenues from customers in the Automotive, Hydraulic and Aerospace sectors from dual sourcing and some Industrial OEM customers were lost because of weaker service delivery caused by operational challenges that arose following the ERP implementation.

In the second half of the year, the principal issues relating to the ERP implementation were successfully resolved with a corresponding and substantial improvement in operational processes. In September, a new leadership team was appointed and the business has now stabilised and is looking forward to resume growth by exploiting newly developed products and additional specialty compounds, as well as rebuilding relationships with engineering departments at several large and mid-size customers.

In **MRO**, the VSP Technologies business, acquired in July 2019, reported a solid contribution to revenues in its initial three months as part of the Group with revenues above last year on a like-for-like-basis and in line with our expectations. The business

continued to gain US market share growth in the transportation segment through its RideTight® programme. The demand for the RideTight® programme and related products has also gained traction internationally. The Group has begun developing cross-selling opportunities with our existing Seals businesses and these will provide good opportunities for growth next year.

International Seals

The International Seals businesses, which account for ca. 39% of Seals revenues, reported a 4% increase in reported and underlying revenues, with activity across European Industrial OEM markets softening in the second half of the year, against a strong comparative last year. During the year FPE Seals, Kubo and M Seals UK commenced work on implementing new ERP systems, all of which are expected to go live during 2020. These new systems will lead to substantial operating efficiencies, including cross selling and inventory management within the International Seals businesses and provide a platform to extend their e-commerce activities.

The FPE Seals and M Seals businesses, with their principal operations in the UK, Scandinavia and the Netherlands, together delivered underlying growth of 5% in revenues on a constant currency basis and after adjusting for the acquisition of DMR Seals in September this year.

The FPE Seals business delivered double-digit underlying growth, benefiting from the continuing improvement in the Oil & Gas market and strong growth in international sales which benefited from additional European sales resources added last year. Revenues also benefited from good growth in its core UK Aftermarket hydraulic seals and cylinder parts business, although a weaker UK construction market led to slower activity in the second half of the year.

In September 2019, FPE Seals acquired DMR Seals, a well established UK distributor of bespoke machined seals and gaskets based in Sheffield and supplying OEMs and MRO companies operating in a broad mix of industries. DMR Seals success has been built on deep technical knowledge, high levels of customer service and flexible machining capabilities and complements well the products and services offered by FPE Seals.

M Seals delivered modest growth in revenue in both the Scandinavian and UK markets, although trading activity softened in the second half of the year. In Scandinavia, solid revenue growth was achieved in Sweden driven by specific customer activity, but this was largely offset by flat revenues in the Danish core markets. In the UK, similarly to FPE Seals, M Seals benefited from the improvement in the Oil & Gas market, with customers expanding activities but this was partly offset by a weaker Industrial OEM market.

Kubo, which operates in Switzerland and Austria, increased underlying revenues by 1% with performance very dependent on local market conditions. In Switzerland, revenues reduced modestly against a strong

comparative, as customers looked to reduce inventories to meet weaker industrial production in 2019 also reflecting the impact from the appreciation in the Swiss franc, relative to the Euro. A new distribution supply agreement for a major supplier expanded both the company's customer base and product range and helped mitigate the weakness in some of its existing markets. In Austria, Kubo reported robust revenue growth, benefiting from a new customer contract gained in the second half of last year.

The Kentek business, with principal operations in Finland and Russia, saw revenues reduce by 1% in Euro terms with competitive trading conditions continuing in both Finland and Russia, reflecting generally tougher end markets. Revenues generated in Russia, which account for ca. 65% of Kentek revenues, reduced slightly in Euro terms as the ongoing impact from international sanctions increasingly hindered trading activity and led to some projects being postponed. In response, Kentek continued to focus on sales of its own-brand filter range and also invested in a new sales branch in the far east of Russia to support the mining and logging sectors. In Finland, Kentek revenues reduced by 4% as sales to Aftermarket customers and other distributors suffered from strong competition in a market hampered by a lack of growth opportunities.

The TotalSeal business in Australia and New Caledonia has core capabilities in industrial gaskets and mechanical seals used in MRO operations in complex, high specification and arduous conditions. The business reported double-digit growth in both Australia and New Caledonia against a weak comparative and benefited from an improving mining sector. The business in New Caledonia was successful in renewing its supply contract with its major international mining customer.

Potential for growth

Successful go-live of second distribution facility for US Aftermarket will provide significant opportunities to grow business by accessing expanded US territories

Stabilise and rebuild the Industrial OEM business and broaden geography and products through acquisition

Substantial opportunities to grow VSP Technologies through new product development, expanded activities outside South-East US and through bolt-on acquisitions

Broaden US Industrial OEM distribution activities using new business development resources to accelerate acquisitions

Build larger and broader businesses in International Seals through acquisition and increased cross-selling in existing businesses

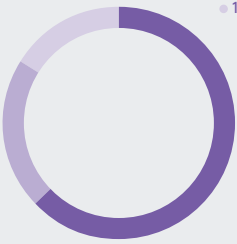


Controls

The Controls Sector businesses supply specialised wiring, cable, connectors, fasteners and control devices used in a range of technically demanding applications

Principal segments

- 63% Interconnect
- 21% Specialty Fasteners
- 16% Fluid Controls



Geography

54%

UK

13%

Rest of world

33%

Continental Europe

Customers

33%

Industrial

7%

Energy & Utilities

30%

Aerospace & Defence

7%

Medical & Scientific

11%

Food & Beverage

1%

Rail

11%

Motorsport

Products

52%

Wire & Cable

10%

Equipment & Components

21%

Fasteners

7%

Control Devices

10%

Connectors

Interconnect

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

Specialty Fasteners

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

Fluid Controls

The Hawco Group businesses supply a range of fluid control products used broadly in the Food & Beverage sector, in applications including food retailing and transportation, catering equipment, vending machines, coffee brewing, pure water and water cooling systems. Products include fluid controllers, compressors, valves,

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

Market drivers

Industrial economic background

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

A good indicator of the health of the UK industrial economy is the UK Index of Production. The index has shown slow, steady growth in recent years until the end of 2017; thereafter activity levels have contracted driven by a weak Manufacturing sector, except for a spike in March 2019 caused by Brexit stockpiling.

In Germany, the Production Sector Output index, following a strong period of recovery through 2010 and 2011, increased steadily until the end of 2017; since 2017, the index has contracted.

In France, industrial production is forecast to grow modestly in 2019 supported by one-off business tax cuts and internal demand, offsetting weaker exports.

Specific industry drivers

Interconnect and Specialty Fasteners

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

Principal operations

Interconnect

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

Specialty Fasteners

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

Hawco Group	Godalming, Bolton & Faringdon, UK
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The Civil Aerospace market continues to grow steadily with growth in world passenger traffic averaging over 7% p.a. over the last five years. Despite a slowdown in order intake during 2019, both Boeing and Airbus have strong order books and Comac continues to develop in China. The ongoing demand for new aircraft is driven by the need to replace ageing fleets with more fuel-efficient aircraft and the demand from airlines in China and the rest of the Asia-Pacific region. There is increased activity in the cabin interiors market, where the wide range of complex seating and entertainment systems is driving growth.

In the Defence sector, the UK remains committed to maintaining the NATO spend target of 2% of GDP and defence spending is forecast to increase by an average of 1.4% p.a. in real terms through to 2020. In Germany, in response to the emergence of new perceived threats and pressure to meet NATO's spending target, the Government has pledged to increase defence spending from ca. 1.3% of GDP in 2018 to ca. 1.5% of GDP in 2024.

In Motorsport, the major drivers of demand in Formula 1 are the number of races and teams (which both remained the same in the 2019 season) and the change in engine design rules. The level of development work related to technology and rule changes were not substantial in the 2019 season. The businesses also supply to other motor racing series, however, the spend is relatively low in these series compared to Formula 1.

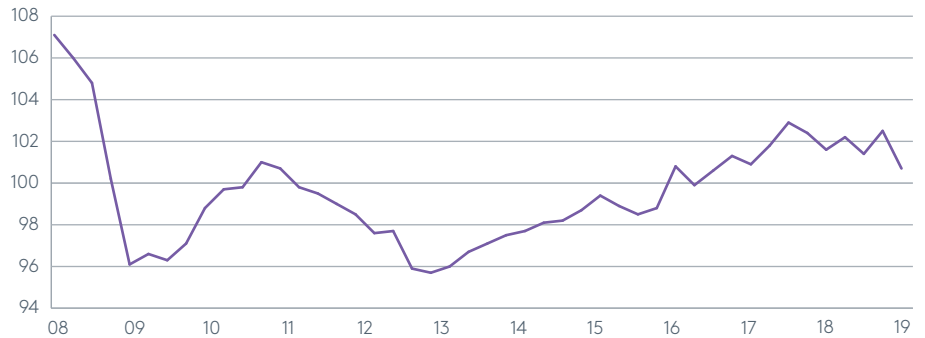
In the UK, the new five-year rail funding control period started in April 2019 and the process to allocate funding for new projects was changed resulting in reduced initial activity. The budget for the new five-year control has been increased to ca. £48bn from £38bn in the previous five-year period. In addition, the Government has undertaken a review of the High Speed Two ("HS2") project, which could delay further investment. In Germany, electricity generation and distribution remains a positive sector due to the fragmented nature of the local supply of electricity, where it is the responsibility of towns and cities.

The UK Construction sector, which is served by the CCA Group, was steadily growing until 2017. Since that point growth has been subdued caused by Brexit uncertainty and the environment remains challenging with new orders also contracting in the second quarter of 2019.

Specific industry drivers – Fluid Controls

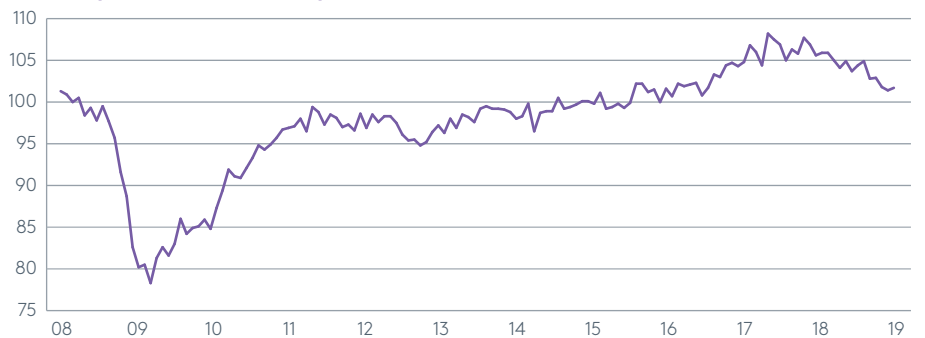
The Fluid Controls businesses generate ca. 70% of their revenues from the Food & Beverage sector in the UK. In Food Retailing, the trend away from major out-of-town stores to convenience stores and home delivery continues. There is also a drive in the Retail industry to reduce energy

UK index of production



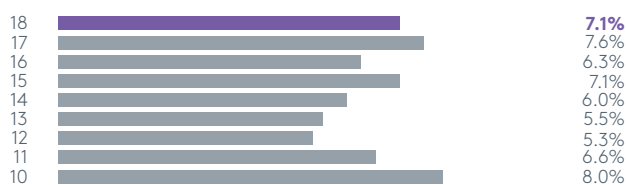
Source: UK Office of National Statistics. GDP estimates in chained volume measures and at current market prices, base year (2015) = 100

German production sector output



Source: Deutsche Bundesbank. Including construction, calendar and seasonally adjusted, reference year 2010 = 100

World passenger traffic (annual growth rate)



Source: International Civil Aviation Organisation.

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

The Coffee market sector saw continued growth of ca. 8% in 2018 and is forecast to grow at ca. 5% p.a. over the next four years with Abbeychart supplying both the coffee machine manufacturers and the Aftermarket sector, predominately in the UK but also in Europe. The Vending market sector continues to see modest growth, driven by the sale of premium products, particularly in the hot drinks segment.

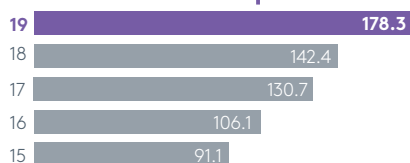
Controls continued

Highlights for the year

- Sector revenue growth of 25%; underlying growth of 9% after adjusting for currency and acquisitions completed both this year and last year
- Interconnect delivered underlying growth of 7% with strong growth in the IS-Group businesses more than offsetting weaker revenues in the CCA Group (Cablecraft and FS Cables)
- The Gremtek acquisition completed in October 2018 adds to the Interconnect business a range of own-branded protective sleeving and cable identification products and expands the business into France
- Clarendon increased underlying revenues by 21%, with growth driven by strong demand from both existing and new Civil Aerospace customers
- Fluid Controls revenues increased by 1% with solid growth in the refrigeration market, held back by a challenging UK industrial market

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

+14% p.a.



Revenue

£178.3m

Sector performance

Reported revenues of the Controls Sector businesses increased by 25% to £178.3m (2018: £142.4m). The acquisition of Gremtek in October 2018 and FS Cables in August 2018, contributed £24.6m or 14% to Sector revenues. After adjusting for negligible currency movements on revenues from translation to UK sterling and for these acquisitions, underlying Sector revenues increased by 9%.

Adjusted operating margins increased by 10bps to 17.7% (2018: 17.6%) largely reflecting operating leverage from strong revenue growth, which more than offset the impact from acquired businesses that joined the Sector at lower initial operating margins. Gross margins improved marginally, largely reflecting mix effects across the Sector businesses. Adjusted operating profits increased by 26% to £31.6m (2018: £25.0m).

Capital expenditure in Controls increased to £2.5m (2018: £1.1m) in 2019, including £0.7m invested in completing the expansion and refurbishment of the IS-Sommer facility in Germany. Contracts to sale and leaseback this facility are expected to be completed in early 2020. In September 2019, £1.3m was invested on a new stand-alone facility for Clarendon to provide additional capacity to meet the substantial growth in this business. After a short period of refurbishment, Clarendon will relocate to this facility in December 2019 before completing a sale and leaseback of the facility early in 2020. Free cash flow increased by 25% to £24.7m (2018: £19.8m) reflecting stronger trading and the benefit from reduced working capital, after the unwinding of Brexit stock built up in the first half of the year.

Interconnect

The Interconnect businesses account for 63% of Controls revenues and reported an increase in revenues of 34% in UK sterling terms. After adjusting for the acquisitions of Gremtek and FS Cables and for currency effects, underlying revenues increased by 7%. Strong underlying growth in the IS-Group and Filcon, more than offset weaker demand in the UK centric CCA Group.

The IS-Group's UK businesses reported a 10% increase in revenues reflecting further success achieved in broadening its customer base across the EMEA region and good growth from sales in the Asia-Pacific region. IS-Group has been successful in the EMEA region by directly targeting cable harness houses and developing its network of

sub-distributors. In the Aerospace sector, a strong performance was driven by sales of assembly tags for fuel pipes, in addition to protective strips and sleeving into an aircraft manufacturer. There was modest fall in the UK Defence sector reflecting the absence of a large one-off order delivered last year. The Industrial sector benefited from a positive first half as customers built inventories ahead of Brexit; however the UK industrial market softened in the second half reflecting weaker economic conditions. The Energy sector remained strong with sales particularly buoyant into offshore and subsea applications and activity levels remaining robust in the North Sea Oil markets. In Motorsport, there was solid revenue growth from an expanding presence in the Formula E race series, which offset another quiet year for development in Formula 1 and WRC. The IS-Cabletec business, a supplier of high performance braided products, also delivered solid growth as it regained business with a key customer.

The IS-Sommer business in Germany delivered 9% growth in revenues with particularly strong performances in the Defence and Energy markets. The improvement in Energy revenues was driven by an expanded territorial access and, an improved service offering to a market with short lead times on inventory availability. In the Defence market, revenue growth was achieved from new projects for the refurbishment of Leopard II tanks and Howitzer (PzH 2000) tanks for supply into Hungary. The Industrial market also grew supported by a large project win for insulation and protection of fuel-pipes into the automotive sector. The Medical sector reported double-digit revenue growth and continued to benefit from technical support provided to manufacturers in previous years to assist them managing new European Regulations for medical devices. Motorsport revenues recovered modestly following a decline in revenues in the prior year when Audi and Volkswagen withdrew from the German DTM series. Aerospace revenues declined in the year against a strong comparative when a new distribution agreement was concluded and led to large initial orders.

In October 2018, IS-Group expanded its European footprint through the acquisition of Gremtek based in Paris, France. Gremtek is a long established and leading supplier of own branded protective sleeving and cable identification products. Now fully integrated into the IS-Group, Gremtek offers a broader

	2019	2018	
Revenue	£178.3m	£142.4m	+25%
Adjusted operating profit	£31.6m	£25.0m	+26%
Adjusted operating margin	17.7%	17.6%	+10bps
Free cash flow	£24.7m	£19.8m	+25%
ROATCE	31.0%	29.8%	+120bps

product range, whilst at the same time providing a platform to sell existing IS-Group products into the French market. Gremtek's revenues since acquisition were in line with expectations.

Filcon reported a 13% increase in revenues against a weak comparative, with strong demand from its three core markets: Military Aerospace, Space and Motorsport. In Military Aerospace, public spending increased in Germany following pressure to meet NATO's defence spending targets. There was strong growth in the Space sector driven by a new customer acquisition and geographic expansion and in Motorsport, demand increased due to new project wins across the existing customer base and the addition of new applications within Formula E.

The CCA Group comprising Cablecraft and FS Cables (acquired in August 2018) together reported a 3% decrease in underlying revenues. Cablecraft revenue suffered from a reduction in demand from the rail sector when the new five-year funding cycle (Control Period 6) opened in April 2019. This led to a combination of a change to the funding process and a delay in commencement of major projects, which are now anticipated to ramp up in early 2020. The wholesale and distribution sectors were also relatively flat as activity levels in the wider construction sector slowed sharply in the second half of the year. During the year, Cablecraft has launched a new e-commerce platform with enhanced functionality providing encouraging indications of revenue growth in the second half of the year from both existing and new customers.

FS Cables, an established and leading supplier of specialist cable products, was acquired in August 2018. The revenues were broadly flat on a like-for-like basis with solid export revenues (which account for ca. 20% of total revenues), offset by weaker revenues in its core UK commercial construction market.

The CCA Group has recently been created to take advantage of cross-selling opportunities across both Cablecraft and FS Cables and to provide a strong platform for future growth under a single leadership team.

Specialty Fasteners

The Clarendon business now accounts for 21% of Controls revenues and reported an increase in underlying revenues of 21%, after adjusting for currency and a small acquisition in the prior year. In a buoyant Civil Aerospace sector, revenue growth continued to be driven by both increased demand from existing customers and further penetration into new customers across Europe and Asia. These customers, along with their sub-contractors, are manufacturing aircraft seating and cabin interiors and Clarendon supports many of these customers by supplying product

through its automatic inventory replenishment system (Clarendon AIR). The number of customers using Clarendon AIR saw significant growth reflecting the high-quality service and responsiveness provided by Clarendon.

In Clarendon's other major market of Motorsport, underlying revenue grew, despite the number of Formula 1 races remaining unchanged and there being no significant changes to engine regulations. Revenues also benefited from demand on "supercar" development projects with major automotive OEMs and from the supply of pre-assembled and captive fasteners and bespoke engineered solutions to the Defence and Industrial sectors.

Clarendon's US business, acquired early last year, delivered robust growth during the year from gaining new customers within the US aircraft seating and cabin interiors sector, as well as solid revenues generated in the space and urban air mobility ("UAM") markets.

Fluid Controls

The Hawco Group of Fluid Controls businesses accounts for 16% of Controls revenues and supplies temperature, pressure and fluid control products, principally to the Food & Beverage industry. Revenues increased by 1% against the prior year with growth coming from the OEM refrigeration market as tighter environmental regulations drove demand; however overall revenue growth was held back by a challenging UK industrial market.

Hawco's revenue growth in the OEM Refrigeration equipment market came from OEMs exporting into the US, supplying into the Refrigerated Transport Home Delivery market and from the ongoing development of store formats in Convenience stores and Petrol forecourts. Contractor revenues were marginally up on prior year with refrigeration spares sales improving, but installation of air conditioning units reduced because of a slowdown in construction projects. Revenues to OEMs for the supply of heating and temperature control products slowed in the financial year as demand weakened and projects were deferred.

Abbeychart revenues declined slightly during the year, where strong revenues from the Coffee, Soft Drinks and Water sectors were more than offset by a weaker Vending sector. In the Vending sector, OEMs reduced production of new machines to match softer demand and operators reduced spare parts held for the Aftermarket. Good progress was made in North America, which delivered growth on the prior year. Additional sales resource was added in the second half of the year to support future growth plans. In May 2019, Abbeychart consolidated its inventory with Hawco's inventory held in Bolton and relocated its operations into a new leasehold facility in Swindon.

Potential for growth

Grow the Interconnect business geographically within Europe and broaden the product offer to include more own branded solutions

Accelerate cross-selling opportunities in CCA Group and maximise sales and marketing channels

Specialty Fasteners will build on strong positions in Civil Aerospace and Motorsport and focus expansion within Europe and the US

Target growth from new refrigeration product in Fluid Controls and drive export business into North America

Finance Review



The Group delivered another year of strong double-digit growth in revenues and adjusted operating profit"

Reported and underlying results in 2019

Reported revenues increased by 12% to £544.7m (2018: £485.1m) and adjusted operating profit increased by 14% to £97.2m (2018: £84.9m). The results benefited from a strong contribution from acquisitions, a currency tailwind and an improvement in adjusted operating margins.

Acquisitions completed this year and last year, net of a small disposal last year, incrementally contributed £26.2m and £4.9m to revenue and adjusted operating profit, respectively. A weakening in UK sterling relative to the US and Canadian dollars, particularly in the second half of the year, provided a currency tailwind of 2% on the translation of the results of the overseas businesses, when compared with last year's average exchange rates. This currency tailwind contributed to an increase in revenues and adjusted operating profits of £9.0m and £1.9m, respectively.

The underlying results present the performance of the Group on a like-for-like basis by adjusting for the contribution from businesses acquired during the year (and from the incremental impact from those acquired last year) and for the impact on the translation of the results of the overseas

businesses from the weakening in the UK sterling exchange rate in the second half of the year, primarily against the US and Canadian dollars. After adjusting for the currency tailwind and for the incremental contribution from acquisitions (net of a small disposal), underlying revenues and underlying adjusted operating profits increased by 5% and 7%, respectively.

Adjusted operating margin

The Group's adjusted operating margin improved by 30bps this year to 17.8% (2018: 17.5%) largely reflecting stronger gross margins from a combination of robust price increases implemented earlier in the financial year, improved focus on other gross margin support costs and tight control of operating costs.

In Life Sciences, adjusted operating margins benefited from strong operational leverage. However, headwinds from adverse currency transactional effects led to slightly weaker gross margins, despite favourable currency hedges partly mitigating the impact from weaker Australian dollar and Canadian dollar spot exchange rates relative to the US dollar and Euro. In Seals, adjusted operating margins remained unchanged as much stronger gross margins from robust price increases to customers and stronger freight

Maintaining financial discipline

Nigel Lingwood
Group Finance Director

ROATCE

22.9%

Free cash flow

£56.5m

Adjusted operating margin

17.8%



recoveries, were offset by increased revenue investments in the US Industrial OEM business to resolve the difficulties with the ERP implementation. In Controls, adjusted operating margins improved marginally reflecting operating leverage from stronger revenues, a small positive mix effect on gross margins, partly offset by initial margin dilution from acquired businesses.

Adjusted and statutory profit before tax

Adjusted profit before tax increased by 14% to £96.5m (2018: £84.8m). The interest expense this year increased to £0.7m (2018: £0.1m), including £0.4m on increased borrowings to finance acquisitions, a small arrangement fee to extend the expiry of the revolver facility and an increase in the notional interest expense on the Group's pension deficit.

Statutory profit before tax was £83.5m (2018: £72.7m) and is after charging acquisition related charges of £13.1m (2018: £9.6m), comprising the amortisation of acquisition related intangible assets and acquisition costs and a net £0.1m credit (2018: £0.4m charge) on the fair value remeasurement of financial liabilities. A one-off charge of £2.1m of CEO transition costs was incurred last year relating to the change of the previous CEO.

Tax charge, earnings per share and dividends

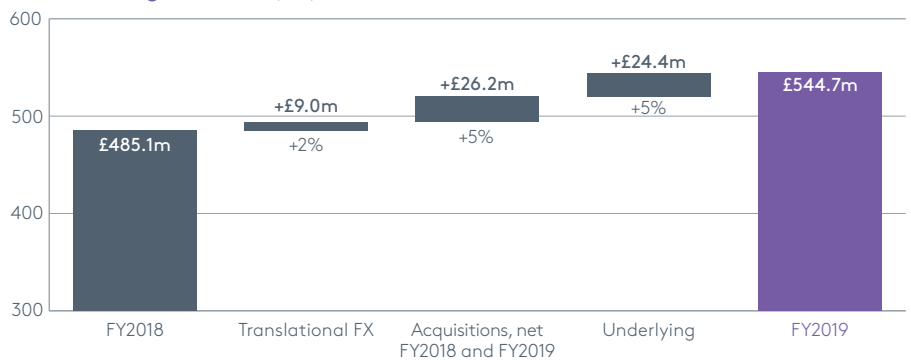
The Group's effective tax charge on adjusted profit remained broadly unchanged at 24.0%, compared with 23.9% last year.

Adjusted earnings per share ("EPS") increased by 14% to 64.3p, compared with 56.4p last year and statutory EPS increased by 15% to 54.7p (2018: 47.5p).

The Board has a progressive dividend policy that aims to increase the dividend each year broadly in line with the growth in adjusted EPS. In determining the dividend in any one year, the Board also considers a number of factors which include the strength of the free cash flow generated by the Group, the future cash commitments and investment needed to sustain the Group's long term growth strategy and the target level of dividend cover. The Board continues to target towards two times dividend cover (defined as the ratio of adjusted EPS to total dividends paid and proposed for the year), which provides a prudent buffer. The ability of the Board to maintain future dividend policy will be influenced by the principal risks identified on pages 28 to 31 that could adversely impact the performance of the Group.

For 2019, the Board has recommended a final dividend of 20.5p per share (2018: 17.8p) making the proposed full year dividend 29.0p (2018: 25.5p). This represents a 14% increase in the proposed full year dividend with dividend cover remaining unchanged at 2.2 times adjusted EPS.

Revenue bridge – FY2019 (£m)



GBP vs G10 currency basket



Free cash flow

Free cash flow represents cash available to invest in acquisitions or return to shareholders. The Group generated strong free cash flow this year of £56.5m compared with £60.5m last year which benefited from £4.0m received on the sale of a small non-core US business. The reduction in free cash flow conversion to 78% (2018: 95%) of adjusted earnings reflects a combination of a larger cash outflow into working capital and increased capital investment this year.

The Group's operating cash flow increased this year by 9% to £92.3m (2018: £84.3m), but was partly offset by both an increase in working capital outflows of £9.4m (2018: £5.1m) and a cash payment of £1.3m (2018: £0.8m) this year to the former CEO in settlement of his compromise agreement. There was a strong inflow of cash from working capital in the second half of the year as the strategic build of inventories at 31 March 2019 to meet both Brexit uncertainty and specific customer/product requirements was successfully unwound by the end of the year. However, the initial difficulties that arose on implementation of the new ERP system in the US Industrial OEM business led to a significant build-up in inventories which was necessary to ensure service levels to customers were maintained. This alone accounted for most of the net increase in inventories of £12.2m (2018: £8.3m) which was partly offset by an inflow of £2.8m (2018: £3.2m) from an increase in net payables at

the year end. The Group's KPI metric of working capital to revenue at 30 September 2019 increased to 16.5% (2018: 15.1%), reflecting the increased inventories held in the US Industrial OEM business at the year end.

Group tax payments increased by £2.9m to £21.9m (2018: £19.0m). On an underlying basis, cash tax payments represented ca. 22% (2018: 22%) of adjusted profit before tax which is slightly below the effective accounting rate reflecting the benefit from tax timing differences. Underlying tax payments are before currency effects from translation and exclude payments for pre-acquisition tax liabilities in acquired businesses.

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

The Group's capital expenditure increased again this year to £10.9m (2018: £6.6m) largely reflecting investment in expanding the Group's facilities, as well as ongoing investment in both new field equipment in the Healthcare businesses and IT infrastructure across the Group to replace legacy IT systems.

Finance Review continued

During the year, £3.2m was invested in a major project for ca. £8m to set up a new distribution facility for the NA Aftermarket business, comprising fit-out of the new leasehold facility in Louisville, Kentucky together with racking and new carousels. In Germany, a further £0.7m was incurred in completing the expansion of the warehouse and offices in IS-Sommer at a total cost of £1.4m. In the UK, Clarendon invested £1.3m in acquiring a new facility in Wootton Bassett which will allow it to relocate from its current facility which is shared with the IS-Rayfast business. Both the IS-Sommer and the Clarendon facility will be sold and leased back to the businesses early in the next financial year.

The DHG business in Life Sciences invested £2.7m (2018: £2.3m) in field equipment to support placements of new surgical equipment in hospitals and diagnostic machines in laboratories. Investment in IT infrastructure was £1.5m which included £0.9m on completing both the new ERP system in the US Industrial OEM Seals business and on commencing new ERP projects in the International Seals businesses. The remaining capital expenditure of £1.6m was invested on new warehouse equipment and tooling across the Group's businesses.

The Company paid the PAYE income tax liability of £1.7m (2018: £1.0m) on the exercise of LTIP share awards in November 2018, in exchange for reduced share awards to participants. In addition, £1.2m (2018: £1.2m) was paid to the Employee Benefit Trust to fund the acquisition of 100,000 ordinary shares in the Company to meet incentive awards.

The Group spent £78.3m (2018: £20.4m) of free cash flow on acquisitions as described below and £30.1m (2018: £27.0m) on paying dividends to both Company and minority shareholders.

Acquisitions completed during the year

The Group invested £77.2m on acquiring new businesses this year and paid a further £1.1m of deferred consideration for businesses acquired last year. As indicated last year, the increasing uncertainty about the future direction of global economies contributed to a greater number of sellers of private businesses to take advantage of several years of robust financial performance and sell their businesses.

With a more receptive M&A market for these businesses the Group completed a record spend on acquisitions this year. After a lengthy structured sale process, the Group completed the acquisition of VSP Technologies in July for initial consideration of £57.2m, net of expenses and cash acquired in the business. VSP Technologies is a leading supplier of high-quality gaskets and fluid sealing products and the acquisition provides an exciting opportunity to extend our Seals activities in North America, consistent with the Group's strategy.

A further three bolt-on businesses were also acquired in the year for aggregate consideration of £20.0m net of acquisition expenses, and cash acquired. In October last year, Gremtex, a small Interconnect business based in Paris, France was acquired for total consideration of £6.9m and in September this year both DMR Seals, based in Sheffield, UK and Sphere Surgical, based in Melbourne, Australia, were acquired for initial consideration of £7.3m and £6.6m, respectively. These three businesses are good examples of Diploma bolt-on acquisitions which provide each of the Sectors an opportunity to extend into new strategically related markets by broadening the existing product offering leading to increased value to shareholders.

These acquisitions added £53.2m to the Group's acquired intangible assets, which represents the valuation of customer relationships that will be amortised over periods ranging from five to 15 years. At 30 September 2019, the carrying value of the Group's acquired intangible assets was £96.1m (2018: £53.6m) and there was an £11.6m (2018: £9.3m) charge this year to amortise these assets.

Goodwill at 30 September 2019 was £155.0m (2018: £128.5m) and included £24.1m relating to those businesses acquired during the year (including fair value adjustments to the assets and liabilities acquired). Goodwill is not amortised but is assessed each year at a Sector level to determine whether there has been any impairment in the carrying value of goodwill acquired. The exercise to assess whether goodwill has been impaired is described in note 10 to the consolidated financial statements. It was confirmed that there was significant headroom on the valuation of this goodwill, compared with the carrying value of goodwill at the year end.

Liabilities to shareholders of acquired businesses

The Group's liability to shareholders of acquired businesses at 30 September 2019 increased by £5.7m to £11.3m (2018: £5.6m) and comprises both put options to purchase outstanding minority shareholdings and deferred consideration payable to vendors of businesses acquired during the last year.

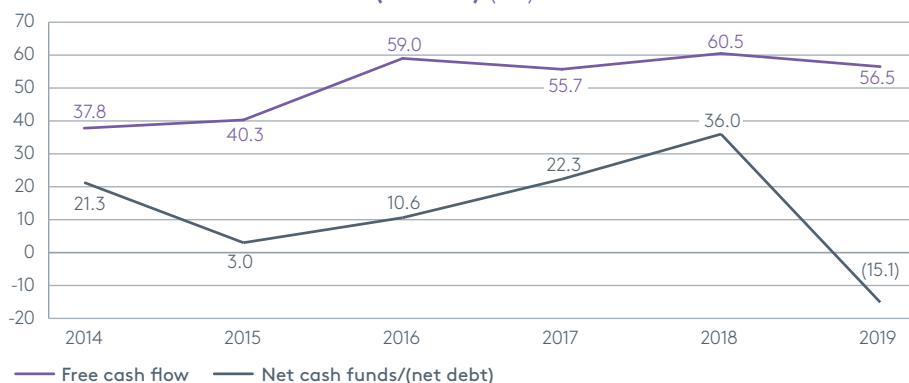
The liability to acquire minority shareholdings outstanding at 30 September 2019 relates to a 10% interest held in both M Seals and Kentek. These options are now fully exercisable and are valued at £4.3m (2018: £4.5m), based on the Directors' latest estimate of the earnings before interest and tax ("EBIT") of these businesses when these options crystallise.

The liability for deferred consideration payable at 30 September 2019 was £7.0m (2018: £1.1m). This liability represents the Directors' best estimate of the amount likely to be paid to the vendors of businesses purchased during the year, based on the expected performance of these businesses during the measurement period. The gross liability for deferred consideration of £7.5m has been discounted to reflect the expected date on which these payments will be made. During the year, £1.1m of deferred consideration was paid to the vendors of Coast and FS Cables that were acquired last year.

Return on adjusted trading capital employed and capital management

A key metric used to measure the overall profitability of the Group and its success in creating value for shareholders is the return on adjusted trading capital employed ("ROATCE"). At a Group level, this is a pre-tax measure that is applied against the fixed and working capital of the Group, together with all gross intangible assets and goodwill, including goodwill previously written off against retained earnings. At 30 September 2019, the Group ROATCE of 22.9% (2018: 24.5%) was weakened slightly by new acquisitions this year but remained comfortably ahead of our 20% benchmark. Adjusted trading capital employed is defined in notes 2 and 3 to the consolidated financial statements.

Free cash flow and net cash funds/(net debt) (£m)



The Group continues to maintain a robust balance sheet with net debt of £15.1m at 30 September 2019, compared with cash funds of £36.0m last year. Surplus cash funds generated in the businesses are generally repatriated to the UK, unless they are required locally to meet certain commitments, including acquisitions.

The Group extended the expiry of its committed revolving multi-currency credit facility this year to 1 June 2022. This facility comprises a £30m committed facility with an accordion option that allows the Group to increase this commitment up to a maximum of £60m of borrowings. It is primarily used to meet any shortfall in cash to fund smaller bolt-on acquisitions. In July this year the Group also drew down on a £40m term facility to help finance the larger acquisition of VSP Technologies, which unless extended under option, is repayable in full by 8 July 2021.

With undrawn facilities of ca. £54m available at 30 September 2019 and negligible debt leverage, the Group remains confident of seeking additional facilities up to a maximum of ca. two times adjusted EBITDA to fund further acquisitions in the new financial year.

Employee pension obligations

Pension benefits to existing employees, both in the UK and overseas, are provided through defined contribution schemes at an aggregate cost in 2019 of £3.8m (2018: £3.1m).

The Group maintains a small legacy closed defined benefit pension scheme in the UK. A formal triennial funding valuation of this scheme was carried out as at 30 September 2016 and reported a funding deficit of £9.2m with a 75% funding level, based on bond yields of 1.5% at the valuation date, compared with 1.8% at 30 September 2019. The Company is currently funding this deficit with cash contributions of £0.5m (2018: £0.5m) which increases annually on 1 October by 2% with the objective of eliminating the deficit within ten years. A charge of £0.1m has also been made against operating profits this year to equalise GMPs accrued between 1990 and 1997, between men and women.

At 1 September 2018, the scheme trustees completed a buy-in of the pensioner liabilities which represented ca. 30% of the scheme's liabilities existing at 1 September 2018. A new formal funding valuation is being carried out as at 30 September 2019 and the results will be reported in next year's Annual Report & Accounts.

In Switzerland, local law requires Kubo to provide a contribution based pension for all employees, which is funded by employer and employee contributions. This pension plan is managed for Kubo through a separate multi-employer plan of non-associated Swiss companies, which pools the funding risk between participating companies. In Switzerland, Kubo's annual cash contribution to the pension scheme was £0.4m (2018: £0.2m).

Both the UK defined benefit scheme and the Kubo defined contribution scheme are accounted for in accordance with IAS19 (Revised). At 30 September 2019, the aggregate accounting pension deficit in these two schemes increased sharply by £7.3m to £17.8m reflecting the impact from a large reduction in bond yields in both the UK and Switzerland during the second half of the year. The gross aggregate pension liability in respect of these two schemes at 30 September 2019 increased by £8.2m to £57.3m, which is funded by £39.5m of assets.

New Reporting Standards (IFRSs)

The Group adopted two new International Financial Reporting Standards (IFRSs) this year: *Revenue from Contracts with Customers* (IFRS15) and *Financial Instruments* (IFRS9). There is no material impact on the consolidated financial statements from adopting these new standards, although additional disclosure has been included in the notes to the consolidated financial statements.

IFRS16 (*Leases*) will be implemented from 1 October 2019. The work carried out to assess the impact of this new standard has indicated that ca. £34m of existing operating leases – referred to as "Right of Use" assets – will be capitalised on the Group Balance Sheet with the obligation to fund these operating leases being recognised as ca. £34m of debt. The impact on adjusted operating profit and adjusted profit before tax is not expected to be material. There will be no impact on the Group's free cash flow.

Impact of Brexit

At an operational level, the impact on the Group's businesses from the current uncertainty over the process and timing of the UK's exit from the European Union is not expected to be significant in terms of the Group's overall profitability. UK based revenues account for 28% of the Group's overall revenues and the UK businesses, as well as those based in Continental Europe, are substantially "in country" industrial suppliers of goods with limited cross border sales activity.

The Group's financial results this year have been slightly impacted by macroeconomic instability caused by the delayed and uncertain timing of the intended exit from the European Union. This uncertainty has contributed to a weaker UK economy and to a substantial depreciation in UK sterling, particularly in the second half of the year. This has had a negative impact on the Group's operating profits, although the overall Group results this year have benefited from the translation of the results of the Group's overseas businesses into UK sterling.

A prolonged disruption at the UK's borders as a result of Brexit has the potential to impact the supply chain of the Group's UK businesses. In the first half of the year the Group's UK businesses extended the depth of inventories by ca. £2m from building inventory levels of their faster moving product lines which was successfully unwound by 30 September 2019. The Board will continue to monitor closely developments in the Brexit plans, but currently has no intention to rebuild inventory levels.

Internal Control and Risk Management

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

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

Our approach

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

The Group's risk management systems are monitored by the Audit Committee, under delegation from the Board. The Audit Committee is responsible for overseeing the

effectiveness of the internal control environment of the Group. An Internal Audit function has been in place for many years to provide independent assurance that the Group's risk management, governance and internal control processes are operating effectively.

Identifying and monitoring material risks

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

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

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

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

Our principal risks and uncertainties

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

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

The Board has again considered the risks associated with the UK's vote to leave the European Union and this is explained further on page 27 in the Finance Review.

Viability Statement – Diploma PLC


The Directors confirm that they have a reasonable expectation that the Group will continue to operate and meet its liabilities, as they fall due, for the next three years to September 2022. The Directors' assessment has been made with reference to the resilience of the Group and its strong financial position, the Group's current strategy, the Board's risk appetite and the Group's principal risks and how these are managed, as described in the Strategic Report. In September 2019, the Board approved a report on an update of the Group's strategy for the three years ending 30 September 2022, as described on pages 8 to 10.

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

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

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

The Directors confirm that this robust assessment also considers the principal risks facing the Group, as described on pages 29 to 31 and the potential impacts these risks would have on the Group's business model, future performance, solvency or liquidity over the assessment period. The Board considers that the diverse nature of the Sectors and geographies in which the Group operates acts significantly to mitigate the impact any of these risks might have on the Group.

Risk	Risk description and assessment	Mitigation
<p>Strategic Risk Downturn/instability in major markets</p> <p>Change</p> 	<p>Adverse changes in the major markets in which the businesses operate can have a significant impact on performance. The effects of these changes can be seen in terms of slowing revenue growth, due to reduced or delayed demand for products and services, or margin pressures due to increased competition.</p> <p>A number of characteristics of the Group's businesses moderate the impact of economic and business cycles on the Group as a whole:</p> <ul style="list-style-type: none"> • The Group's businesses operate in three differing Sectors with different cyclical characteristics and across a number of geographic markets. • The businesses offer specialised products and services, which are often specific to their application; this offers a degree of protection against customers quickly switching business to achieve a better price. • A high proportion of the Group's revenues comprise consumable products that are purchased as part of the customer's operating expenditure, rather than through capital budgets. • In many cases the products are used in repair, maintenance and refurbishment applications, rather than original equipment manufacturer. • The global economic outlook was more uncertain towards the end of the financial year. 	<p>The businesses identify key market drivers and monitor the trends and forecasts, as well as maintaining close relationships with key customers who may give an early warning of slowing demand.</p> <p>Changes to cost levels and inventories can then be made in a measured way to mitigate the effects.</p> <p>Significant global events are closely monitored to determine any potential impact on key markets.</p>
<p>Strategic Risk Supplier concentration/loss of key suppliers</p> <p>Change</p> 	<p>For manufacturer-branded products, there are risks to the business if a major supplier decides to cancel a distribution agreement or if the supplier is acquired by a company that has its own distribution channels in the relevant market. There is also the risk of a supplier taking away exclusivity and either setting up direct operations or appointing another distributor.</p> <p>Currently no single supplier represents more than 10% of Group revenue and only four suppliers represent more than 2% each of Group revenue.</p> <p>Relationships with suppliers have normally been built up over many years and a strong degree of interdependence has been established. The average length of the principal supplier relationships in each of the Sectors is over ten years.</p> <p>The strength of the relationship with each supplier and the volume of activity generally ensures continuity of supply, when there is shortage of product.</p> <p>The success of the businesses depends significantly on representing suppliers whose products are recognised in the marketplace as the leading competitive brand. If suppliers fail to support these products with new development and technologies, then our businesses will suffer from reduced demand for their products and services.</p>	<p>Long term, multi-year exclusive contracts signed with suppliers with change of control clauses, where possible, included in contracts for protection or compensation in the event of acquisition.</p> <p>Collaborative projects and relationships maintained with individuals at many levels of the supplier organisation, together with regular review meetings and adherence to contractual terms.</p> <p>Regular review of inventory levels.</p> <p>Bundling and kitting of products and provision of added value services.</p> <p>Periodic research of alternative suppliers as part of contingency planning.</p> <p>The businesses work very closely with each of their suppliers and regularly attend industry exhibitions to keep abreast of the latest technology and market requirements/trends. The businesses also meet with key customers on a regular basis to gain insight into their product requirements and market developments.</p>
<p>Strategic Risk Customer concentration/loss of key customer(s)</p> <p>Change</p> 	<p>The loss of one or more major customers can be a material risk.</p> <p>The nature of the Group's businesses is such that there is not a high level of dependence on any individual customer and no single customer represents more than 3.5% of Sector revenue or more than 1.5% of Group revenue.</p>	<p>Specific large customers are important to individual operating businesses and a high level of effort is invested in ensuring that these customers are retained and encouraged not to switch to another supplier.</p> <p>In addition to providing high levels of customer service and value-added activities, close integration is established where possible with customers' systems and processes.</p>

Internal Control and Risk Management continued




Risk	Risk description and assessment	Mitigation
Operational Risk Cybersecurity/ information technology/ business interruption	<p>Group and operating business management depend critically on timely and reliable information from their IT systems to run their businesses. The Group seeks to ensure continuous availability, security and operation of those information systems.</p> <p>Cyber threats to the businesses information systems have this year reduced, following action taken to strengthen the IT infrastructure environment across the Group's businesses.</p> <p>Any disruption or denial of service may delay or impact decision making through lack of availability of reliable data. Poor information handling or interruption of business may also lead to reduced service to customers. Unintended actions of employees caused by a cyber-attack may also lead to disruption, including fraud.</p> <p>The North American Aftermarket business is operated from a single warehouse based in Tampa, Florida which continues to be exposed to hurricanes during the season from August to November.</p> <p>The US Industrial OEM Seals business experienced difficulties with implementation of a new ERP system earlier in the year.</p>	<p>There is good support and back-up built into local IT systems and the spread of businesses with their own stand-alone IT systems also offers good protection from individual events. The majority of businesses back-up online data at least once a day to an offsite data storage centre.</p> <p>A member of the Executive Management Committee is responsible for ensuring each business in the Group has a robust cybersecurity programme and reports twice a year to the main Board on the status of cybersecurity across the Group. In addition, education/awareness of cyber threats continues to ensure Group employees protect themselves and Group assets. At 30 September 2019, all businesses had achieved the UK Government endorsed Cyber Essentials accreditation; it is expected that recently acquired businesses will be fully accredited in 2020.</p> <p>Business continuity plans exist for each business with ongoing testing.</p> <p>The North American Aftermarket Seals business is investing in a second facility in Louisville, Kentucky.</p> <p>In response to the ERP implementation difficulties in 2019, the Group has set up a committee to oversee more closely the processes and milestones during any future ERP implementation across the Group.</p>
Operational Risk Loss of key personnel	<p>The success of the Group is built upon strong, self-standing management teams in the operating businesses, committed to the success of their respective businesses. As a result, the loss of key personnel can have an impact on performance, for a limited time period.</p> <p>The average length of service of the ca. 110 senior managers in the Group is ten years and for all personnel in the Group is consistently ca. seven years.</p>	<p>Contractual terms such as notice periods and non-compete clauses can mitigate the risk in the short term. However, more successful initiatives focus on ensuring a challenging work environment with appropriate reward systems. The Group places very high importance on planning the development, motivation and reward for key managers in the operating businesses including:</p> <ul style="list-style-type: none"> • Ensuring a challenging working environment where managers feel they have control over, and responsibility for, their businesses. • Establishing management development programmes to ensure a broad base of talented managers. • Offering a balanced and competitive compensation package with a combination of salary, annual bonus and long term cash or share incentive plans targeted at the individual business level. • Giving the freedom, encouragement, financial resources and strategic support for managers to pursue ambitious growth plans.

Change



Change



Risk	Risk description and assessment	Mitigation
<p>Operational Risk Product liability</p>	<p>There is a risk that products supplied by a Group business may fail in service, which could lead to a claim under product liability.</p>	<p>Technically qualified personnel and control systems are in place to ensure products meet quality requirements. The Group's businesses are required to undertake Product Risk assessments and comprehensive Supplier Quality Assurance assessments. The Group has also established Group-wide product liability insurance which provides worldwide umbrella insurance cover of £30m across all Sectors.</p>
<p>Change </p>	<p>If a legal claim is made it will typically draw in our business as a party to the claim and the business may be exposed to legal costs and potential damages if the claim succeeds and the supplier fails to meet its liabilities for whatever reason. Product liability insurance can be limited in terms of its scope of insurable events, such as product recall.</p> <p>In situations where a Group business is selling own-branded products and cannot subrogate the liability to a supplier, the business will be liable for failure of the product. A Group business may also be liable for the associated costs of a subsequent customer recall arising directly from failure of an own-branded product.</p>	<p>The businesses, in their terms and conditions of sale with customers, will typically mirror the terms and conditions of purchase from the suppliers. In this way the liability can be limited and subrogated to the supplier.</p> <p>The Group's businesses have undergone product liability training and are continually reviewed to demonstrate compliance with Group policies and procedures relating to product liability.</p>
<p>Financial Risk Foreign currency</p>	<p>Foreign currency risk is the risk that currency rates will affect the Group's results. The Group is exposed to two types of financial risk caused by currency volatility: translational exposure, being the effect that currency movements have on the Group's financial statements on translating the results of overseas subsidiaries into UK sterling; and transactional exposure, being the effect that currency movements have on the results of operating businesses because their revenues or product costs are denominated in a currency other than their local currency.</p>	<p>The Group operates across a number of diverse geographies but does not hedge translational exposure of operating profit and net assets.</p>
<p>Change </p>	<p>The Group operates internationally and is exposed to translational foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar, the Canadian dollar, the Australian dollar and the Euro. The results and net assets of the Group's operations outside the UK are also exposed to foreign currency translation risk.</p> <p>A strengthening of UK sterling by 10% against all the currencies in which the Group does business, would reduce adjusted operating profit before tax by approximately £7.4m (8%), due to currency translation. Similarly, a strengthening of UK sterling by 10% against all the non-UK sterling capital employed would reduce shareholders' funds by £13.8m (5%).</p> <p>The Group's UK businesses are exposed to transactional foreign exchange risk on those purchases that are denominated in a currency other than their local currency, principally US dollars and Euros. The Group's Canadian and Australian businesses are also exposed to a similar risk as the majority of their purchases are denominated in US dollars and Euros. The Group's US businesses do not have any material foreign currency transactional risk.</p>	<p>The Group's businesses may hedge up to 80% of forecast (for a maximum of 18 months) foreign currency transactional exposures using forward foreign exchange contracts.</p> <p>The Group finance department monitors rolling monthly forecasts of currency exposures.</p> <p>Details of average exchange rates used in the translation of overseas earnings and of year end exchange rates used in the translation of overseas balance sheets, for the principal currencies used by the Group, are shown in note 28 to the consolidated financial statements.</p>
<p>Accounting Risk Inventory obsolescence</p>	<p>Working capital management is critical to success in specialised industrial distribution businesses as this has a major impact on cash flow. The principal risk to working capital is in inventory obsolescence and write-off.</p>	<p>Inventory write-offs are controlled and minimised by active management of inventory levels based on sales forecasts and regular cycle counts.</p>
<p>Change </p>	<p>The charge against operating profit in respect of aged or surplus inventory in the year was £2.1m, but inventories are generally not subject to technological obsolescence.</p>	<p>Where necessary, a provision is made to cover both excess inventory and potential obsolescence.</p>

Corporate Responsibility

Our employees

The Board recognises that building and developing the skills, engagement and culture of the growing workforce, are essential to achieving the Group's success. Succession planning is also important as the Group grows and mitigates the principal risk, set out on page 30, which can arise from the loss of key personnel and their associated knowledge, skill and experience. The average length of service, which remains consistently high at ca. seven years, reflects the stability and commitment of the employees. Staff turnover remains modest at ca. 20% whilst the number of working days lost to sickness has increased slightly to ca. 2% a year. These measures remain consistent across each of the Group's Sectors.

Key employee statistics

	2019	2018	2017
Average number of employees in year	1,896	1,765	1,658
Females as percentage of total	35%	35%	35%
Length of service (years)	6.7	6.8	6.7
Average staff turnover	19.8%	19.7%	20.6%
Sick days lost per person	4.1	3.6	3.3

The Group encourages good physical and mental health, but has seen an increase in the number of sick days lost per person this year. This is mostly due to specific, limited employee situations impacting both long and short term absence from work.

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

	2019			2018		
	Male	Female	Total	Male	Female	Total
Directors	5	1	6	4	1	5
Senior managers	89	22	111	78	18	96
Employees	1,244	707	1,951	1,092	614	1,706
Total	1,338	730	2,068	1,174	633	1,807

Gender diversity in the Group is very important and currently ca. 35% of the Group's employees are female. The Board continues to encourage and support greater diversity at all levels in the Group's businesses.

The Group values the commitment of its employees and recognises the importance of communication in fostering good working relationships. The Group keeps employees informed on matters relating to their employment, business developments, successes, and financial and economic factors affecting the Group. This is achieved through videos, management briefings, internal announcements, the Group's website and by the distribution of Preliminary and Interim Announcements and press releases. Copies of the Annual Review and Annual Report & Accounts are also made available in the operating businesses and provide employees an understanding of the Group's business objectives and their roles in achieving them.

Both employment policy and practice in the Group are based on non-discrimination and equal opportunities. Ability and aptitude are the determining factors in the selection, training, career development and promotion of all employees.

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

Employment policies throughout the Group have been established to comply with relevant local legislation and codes of practice relating to employment, Health & Safety and equal opportunities. The Group provides good quality working environments and facilities for employees, and training and development appropriate to each of their roles.

The Group provides sponsorship for high potential employees for higher education courses, where appropriate, and employees are actively encouraged to undertake Continuing Professional Development ("CPD"). Some of the Group's operating companies have structured apprenticeship schemes of which nine (2018: ten) were undertaken in the UK this year.

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

Health & Safety

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

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

Health & Safety forms part of the induction process for new employees and, where relevant, more specialist training is provided for specific functions. The Group has good coverage of employees who have formal Health & Safety training and/or qualifications, and this has continued to increase during 2019.

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

	2019	2018	2017
Near misses	88	73	70
Minor injuries	101	71	56
Reportable lost time incidents ¹	9	1	5
Minor injuries per 1,000 employees	62.8	40.2	33.8
Reportable lost time incidents ¹ per 1,000 employees	4.7	0.6	3.0

¹ Three or more days' absence from workplace.

The absolute levels of minor injuries and near misses have increased this year but are seen as an indication of more diligent reporting practices. The near miss reporting system has placed emphasis on the need to identify and implement corrective actions prior to incidents occurring, which assists with reducing Health & Safety risk. The number of reportable lost time incidents has increased although the majority of incidents resulted in fewer than five lost days. All incidents are fully investigated, and corrective actions and preventative measures are put in place to ensure that the incident does not reoccur, and future risks are mitigated.

Human rights

The Group's activities are substantially carried out in developed countries that have strong legislation governing human rights. The Group complies fully with appropriate legislation in the countries in which it operates to ensure the rights of every employee are respected and all stakeholders are treated with dignity and respect. The Group promotes employment practices to ensure fair regard to diversity and equal opportunities. Staff are provided with a safe, secure and healthy environment in which to work. Employees have access to an independent hotline to report any issues relating to Human Rights violations.

Modern slavery

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

Environmental matters

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

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

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

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

Greenhouse gas emissions

UK listed companies are required to report their global levels of greenhouse gas ("GHG") emissions in their annual report and accounts. This requirement is for disclosure of Scope 1 (direct) and Scope 2 (indirect) emissions and only to the extent that such emissions are the responsibility of the company; direct emissions include heating, cooling and transport fuel and examples of indirect include purchased electricity.

The Group has considered the six main GHGs and report emissions in tonnes of CO₂ equivalent ("CO₂e") for both Scope 1 (direct) and Scope 2 (indirect) emissions. These emissions are calculated following the GHG Protocol and UK Government Environmental Reporting Guidelines. The Group has used Defra UK GHG Conversion Factors, US Environmental Protection Agency Emission Factors and International Energy Agency Factors.

As a distributor with no owned logistics or freight, the Group's primary direct energy usage and related CO₂ emissions arise from the Group's facilities. Where possible the Group has reported billed data which represents ca. 80% of the Group's global emissions. For the remaining entities the Group has used an estimation using sales data and local conversion factors.

An intensity ratio of CO₂e per £1m revenue has been selected, which will allow a comparison of performance over time and with other similar types of business.

Source of emissions	Tonnes of CO ₂ e	
	2019	2018
Direct emissions (Scope 1)		
Natural gas	907	726
Owned transport	95	65
Indirect emissions (Scope 2)		
Electricity	3,281	2,682
Gross emissions	4,283	3,473
Tonnes CO ₂ e per £1m revenue	7.9	7.2

Task Force on Climate-related Financial Disclosures ("TCFD")

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

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

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

Business ethics, corruption and bribery

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

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

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

The Group also maintains processes and policies to monitor and review compliance across the Group's businesses in connection with anti-bribery/corruption and international sanctions.

Community

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

The Group's businesses contribute to their local communities through numerous charitable and fundraising activities, primarily in support of health and children's charities.

The Group also contributes to local worthwhile causes and charities and in 2019 the Group made donations to charitable organisations of £46,441 (2018: £47,221). No political donations were made.

Board of Directors

01

John Nicholas^{1,3} Chairman

Appointed: Joined the Board on 1 June 2013 and appointed Chairman on 21 January 2015.

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

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

External appointments: John is non-Executive Chairman of Porvair plc.

02

Johnny Thomson Chief Executive Officer

Appointed: Joined the Board on 25 February 2019 as Chief Executive Officer.

Skills and experience: Johnny worked with Compass Group PLC for nine years to the end of 2018, with the last three years as Group Finance Director and a member of the Board of Compass Group PLC. He has also been Regional Managing Director of both Latin America and CAMEA (Central Asia, Middle East & Africa).

Johnny began his career at PricewaterhouseCoopers LLP after which he joined Hilton Hotels in a senior executive role. Johnny has lived and worked in Europe, North America, Asia and across Latin America.

External appointments: None.

03

Charles Packshaw^{1,2,3} Senior Independent Non-Executive Director

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

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

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

04

Nigel Lingwood Group Finance Director

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

Will retire from the Board before 30 September 2020.

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

External appointments: None.

05

Anne Thorburn^{1,2,3} Non-Executive Director

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

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

External appointments: Anne is a non-Executive Director of TT Electronics plc.

06

Andy Smith^{1,2,3} Non-Executive Director

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

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

External Appointments: None.

Committee membership

1 Remuneration Committee

2 Audit Committee

3 Nomination Committee

01



02



03



04



05



06



Corporate Governance

// Succession planning and appointment of senior leadership is a critical responsibility of the Board."

John Nicholas
Chairman



Members of Board	Attendance
Chairman	
John Nicholas	11/11
Independent non-Executive Directors	
Andy Smith	11/11
Charles Packshaw	11/11
Anne Thorburn	11/11
Executive Directors	
Johnny Thomson	5/5
Nigel Lingwood	11/11

Dear Shareholder

Succession planning and appointment of senior leadership is a critical responsibility of the Board. We were very pleased to appoint Johnny Thomson as Chief Executive Officer in January this year and it was particularly helpful to the Group's businesses that he was able to start work with them from February. Johnny brings a wealth of experience gained from a much larger company and has made good progress in preparing the Diploma organisation for future growth. In September, the Board had no hesitation in confirming their support for Johnny's refreshed strategy for the Group that we were pleased remained based on the strong foundations of the previous strategy which has proved to be resilient and very successful over many years.

As the year closes, the Board continues with its focus on succession planning with its search for a new non-Executive Director to join the Board and its support of Johnny and our new Group HR Director in seeking a successor to Nigel Lingwood, our long-standing Group Finance Director.

The changes in Executive Board leadership of the Group has encouraged the Board to ask our Remuneration Committee Chairman to bring forward by one year the triennial review of the Company's Remuneration Policy. The new Policy has been updated to reflect both the changes in recent corporate governance regulation regarding Executive remuneration and recognition that the Group is now almost twice the size it was when the Policy was last reviewed. Details of these proposed changes to the Company's Policy are set out by the Remuneration Committee Chairman in the Policy Change Table on page 48 of this Annual Report & Accounts.

The Audit Committee Chair has also been busy this year with making sure that new financial reporting standards which impact both this year's and next year's financial statements have been properly implemented and the impact fully explained. Again more details on these matters and other work carried out by the Audit Committee during this year is set out on pages 41 to 44.

The Board and its Committees are now setting up processes to apply the new requirements set out in the 2018 UK Corporate Governance Code and I look forward to reporting on these exercises in next year's Annual Report & Accounts.

I hope that as shareholders in the Company you will be able to find time to attend our AGM on Wednesday, 15 January 2020 to meet the Board of Directors and challenge them on any matters you feel are important to the future development of the Group.

John Nicholas
18 November 2019

FRAMEWORK OF CORPORATE GOVERNANCE

The Board

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

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

Where appropriate, matters are delegated to a Committee, which will consider them in accordance with its Terms of Reference. Details of each Committee's Terms of Reference are available on the Diploma PLC website at www.diplomaplc.com/governance/constitutional-documents.

Audit Committee

Chaired by Anne Thorburn

Number of meetings in the year: eight

Role of the Committee

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

Nomination Committee

Chaired by John Nicholas

Number of meetings in the year: six

Role of the Committee

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

Remuneration Committee

Chaired by Andy Smith

Number of meetings in the year: 11

Role of the Committee

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

Leadership

Board composition

The Board comprises a Chairman, two Executive Directors and three independent non-Executive Directors. The non-Executive Directors are appointed for specified terms and the details of their respective appointments are set out in the Remuneration Committee Report on page 53. The biographical details of the Board members are set out on pages 34 and 35.

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

Activities of the Board

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

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

COMPLIANCE WITH THE CODE

Diploma PLC is required to state how it has applied the Main Principles of the UK Corporate Governance Code ("the Code"), issued by the Financial Reporting Council ("FRC") in April 2016. Set out on pages 38 to 40 is an explanation of how the Company has applied the Main Principles of the 2016 Code.

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

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

Chairman until a new Chief Executive Officer was appointed. Johnny Thomson was appointed Chief Executive Officer on 25 February 2019, at which time John Nicholas stepped down as interim Executive Chairman.

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

In July 2018, the FRC issued a new Code which will be mandatory for the Company in respect of the year beginning on 1 October 2019. The Board has assessed its governance practices against the provisions of the new Code during 2019 and will report on its implementation in next year's Annual Report & Accounts.

Corporate Governance continued

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

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

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

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

To ensure that non-Executive Directors can constructively challenge and support proposals on strategy, the Board has adopted a process of reviewing and approving the agreed strategy for the Company on a three-yearly basis. The Board met in September 2019 and formally reviewed and approved the Company's strategy.

Meetings of the Board

The Board has seven scheduled meetings during the financial year but will meet more frequently if required. In 2019 the Board had an additional four meetings largely as a consequence of matters relating to the departure and subsequent appointment of the Chief Executive Officer.

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

The Board ensures that at least one of the scheduled meetings is held on site at one of the Group's facilities, where the Board has an opportunity to both receive presentations from local management and meet employees of that business. In March 2019, the Board's scheduled meeting was held at Techno-Path (Distribution) Limited ("TPD") facility in Ballina, Co. Tipperary, Ireland. At this meeting the Board received presentations from senior management in TPD and had an opportunity to view the facility and meet with employees to gain a better understanding of the products and operations managed from this facility.

In September 2019, the Board approved a report on the Group's strategic objectives for the three years ending 30 September 2022. This report was prepared on a top down basis by the Chief Executive Officer with substantial input from the Chief Executives of all of the Group's Sectors and supported by a detailed financial model which was used to assess different scenarios over the strategy period.

Effectiveness

Independent non-Executive Directors

The non-Executive Directors are determined by the Board to be independent in character and judgement and there are no relationships or circumstances that could affect, or appear to affect, a Director's judgement. The Chairman, John Nicholas, was considered independent by the Board both at the time of his appointment as Director on 1 June 2013 and as Chairman on 21 January 2015. John Nicholas was appointed interim Executive Chairman on 28 August 2018 following the departure of the previous Chief Executive Officer, until 25 February 2019 when Johnny Thomson was appointed Chief Executive Officer.

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

Each non-Executive Director is required to inform the Board of any changes to their other appointments and from 1 October 2019, all such appointments will require prior Board approval.

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

The appointment of non-Executive Directors is subject to formal, rigorous and transparent procedures which are described more fully in the Nomination Committee Report set out on page 45.

Diversity

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

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

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

The Board supports the recommendations of the Hampton-Alexander review on gender diversity but believes that other types of diversity are equally important. The Board is currently diverse across a range of criteria, but it is committed to strengthen that diversity, including gender and ethnic diversity, when appropriate opportunities arise. The Board will also take account of its objective to meet the Hampton-Alexander review targets before the end of the next Board rotation of non-Executive Directors. During 2019, the Board commenced a search process to appoint an additional non-Executive Director with relevant experience and diversity qualities. When concluded the Board will meet the Hampton-Alexander diversity targets.

Information and professional development

An induction programme is agreed for all new Directors aimed at ensuring that they are able to develop an understanding and awareness of the Group's core processes, its people and businesses. The non-Executive Directors' awareness of the businesses is further developed through periodic visits to the principal business locations and presentations to the Board by senior management of the businesses. In 2019, the Board received presentations from the Chief Executives of the Seals Sector and the Life Sciences Sector and from management of the TDP business.

Following a new appointment to the Board, a managed induction programme is arranged that includes a visit by the Director to the major business units in each of the Group's Sectors where they have an opportunity to meet with senior management in these businesses. Meetings are held individually between each of the non-Executive Directors and the Executive Directors and with some of the principal advisors to the Company. A managed and thorough induction programme was arranged following the appointment of Johnny Thomson as Chief Executive Officer in February 2019. This programme provided for one-to-one meetings with members of the Board, senior members of the Company and key advisors to the Company, together with substantive visits to the Group's principal businesses.

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

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

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

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

Board evaluation

The Board undertakes an externally led evaluation of the effectiveness of the Board every three years, in accordance with the Code. This exercise encompasses an evaluation of the Board as a whole, the Board Committees and of individual Directors of the Company. The most recent external evaluation was carried out in August 2018 and was externally led by Clare Chalmers, who had no other connection with the Company. The external facilitator interviewed the Directors and the Group Company Secretary. The evaluation also included a review of the Annual Report & Accounts, with particular focus on the corporate governance section. There was also a review of the Board and Committee meeting papers, including minutes of each meeting. A written report was provided to and discussed with the Board Directors that concluded that the Board had a collegiate culture led by a capable and experienced Chairman; it added that there were sound governance processes, with a successful and well-supported Remuneration Policy and that there was good and detailed financial reporting. The actions arising from the 2018 evaluation were reviewed by the Board, which noted that the recommendations to invite senior management and advisors to present to the Board and the appointment of a Group HR Director had been carried out.

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

The Board carried out an internal evaluation of performance in 2019 and the Chairman discussed the results for 2019 with the Board. The Board agreed the actions for 2020 to include a review of the content of Board papers, with increased focus on insight and consideration of the new requirements on governance. On employee engagement, the actions included the development of a people plan, increased employee communications and to conduct an all employee survey early in 2020.

The Senior Independent Director, together with the non-Executive Directors also carries out each year (and has done so in 2019), a performance evaluation of the Chairman, having taken account of the views of all of the Directors.

Powers of the Directors

The Board of Directors is responsible for the management of the business of the Company and may exercise all the powers of the Company, subject to the Articles, the Companies Act 2006 and any directions given by the Shareholders by special resolution.

Appointment and re-election of Directors

The appointment and replacement of Directors is governed by the Articles of the Code ("the Code"), the Companies Act 2006 and related legislation. Directors can be appointed by the Board or by the Company by ordinary resolution at a general meeting. A Director appointed by the Board will hold office until the next AGM and shall be eligible for election at that meeting. Each Director, being eligible, offers himself for election or re-election at each AGM, in accordance with the Code. The Company can remove a Director from office, including by passing a special resolution or by notice being given by all the other Directors.

Liability insurance

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

Professional advice

A policy is in place pursuant to which each Director may obtain independent professional advice at the Company's expense in furtherance of their duties as a Director of Diploma PLC. A formal request was made during the year when advice was sought in relation to Board succession. In addition, each of the Committees are authorised, through their Terms of Reference, to seek advice at the Company's expense. Early in the year, substantial advice was sought by the Chairman of the Remuneration Committee in relation to the financial settlement in connection with the departure of the Chief Executive Officer and for the appointment of a new Chief Executive Officer.

Corporate Governance continued

Conflicts of interest

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

The Company has procedures in place for managing conflicts of interest. Should a Director become aware that they, or any of their connected parties, have an interest in an existing or proposed transaction with the Company, they should notify the Board in writing or at the next Board meeting. Internal controls are in place to ensure that any related party transactions involving Directors, or their connected parties, are conducted on an arm's length basis. Directors have a continuing duty to update any changes to these conflicts.

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

Accountability

The Board is responsible for ensuring that the Annual Report & Accounts taken as a whole present a fair, balanced and understandable assessment of the Group and provides the information necessary to shareholders to assess the Group's position and performance, business model and strategy. The Board receives a detailed Report from the Group Finance Director which sets out the key matters that impact, or could impact the Group's financial statements and Annual Report and highlights areas of the financial statements where it has been necessary to rely upon a significant level of subjectivity. The Board also has access to all relevant information and reviews other periodic management information and RNS announcements. The draft Annual Report & Accounts are circulated to each member of the Board in sufficient time to allow challenge of the disclosures where necessary. The Directors' responsibilities statement is set out on page 61.

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

The principal risks which the Board has identified this year are set out in the section on Internal Control and Risk Management on pages 28 to 31 of the Strategic Report.

Relations with shareholders

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

In addition, Investor Roadshows are now held each year in the US and Canada as well as in the UK and formal investor presentations are made twice a year to groups of private client fund managers.

The Company also engages with existing and potential new investors through a formal Capital Markets Day at which attendees have an opportunity to meet with senior management in the Group to gain a better understanding of the businesses' product portfolios. The last Capital Markets Day was held in London in February 2017.

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

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

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

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

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

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

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

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

Audit Committee Report

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The Group continues to maintain a culture of robust and effective systems of internal control, overseen by strong and experienced finance departments."

Anne Thorburn
 Chair of the
 Audit Committee



Members of Committee	Attendance
Anne Thorburn (Chair)	8/8
Charles Packshaw	8/8
Andy Smith	8/8

Dear Shareholder

This year the Committee focused more of its time on the potential impact on the Group's financial statements from the implementation of new International Reporting Standards ("IFRSs"), following a period of stability with very little change to financial reporting standards.

This year's financial statements reflect the impact from adopting two new IFRSs; IFRS15 on Revenue recognition and IFRS9 on Financial Instruments. As we reported last year, IFRS15 has had no material impact on either the timing or amounts of revenues recognised during the year. Similarly the adoption of IFRS9 has not materially impacted this year's financials statements. However, both standards have led to more detailed disclosure regarding the components of revenue and the basis of providing against receivables which potentially may not be recoverable.

In March this year, the Committee received a report from the Group finance team that set out a detailed evaluation of the potential impact that the new standard on leases may have on the Group's financial statements. The report, which in September was confirmed through more detailed work carried out with the individual businesses, indicates that adoption of this standard will result in ca. £34m of existing operating leases – now referred to as "Right of Use Assets" – being capitalised on the Group's Balance Sheet, with the obligation to fund these operating leases being recognised as £34m of debt. The impact on both adjusted operating profit and adjusted profit before tax will not be material and the adoption of this standard has no impact on the Group's existing cash flows. Further details of the impact is set out in the note on Accounting Policies in the Group's financial statements.

The Committee received a letter from the FRC in May 2019 which confirmed that they had completed a formal review of the Group's 2018 Annual Report & Accounts. I am pleased to report that the letter contained no points that required a formal response.

The Committee again received a report from the Head of Group Tax & Treasury during the year, which included a report on how the Group would manage the requirements of the new legislation on Corporate Criminal Facilitation of Tax Evasion. The tax environment and tax demands on business continues to be increase but the Group continues to maintain strong compliance with local tax legislation and demonstrates good tax governance.

As Chair of the Committee, I continue to meet regularly with members of the Internal Audit team and with Chris Burns from PwC to discuss their reports and gain a closer insight into the finance functions and processes across the Group. This provides me with greater insight of the culture of the internal control environment in the Group and provides assurance that controls are both in place and are tested, which is particularly important given the Group's decentralised operating model.

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

I look forward to meeting shareholders at the AGM on 15 January 2020 and will be happy to respond to any questions relating to the activities of the Audit Committee.

Anne Thorburn
 18 November 2019

Audit Committee Report continued

KEY DUTIES AND FOCUS IN 2019

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

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

- Reviewed and agreed the scope of audit work to be undertaken by the external auditor and agreed the terms of engagement and fees to be paid for the external audit.
- Reviewed the Annual Report & Accounts and received reports from the Group Finance Director and the external auditor on the key accounting issues and areas of significant judgement.
- Reviewed the report on compliance with the UK Corporate Governance Code 2016 and reports on the provision of information to the auditor.
- Reviewed the report from the Group Finance Director on the controls in place to mitigate fraud risk.
- Reviewed the Half Year Announcement and received reports from the Group Finance Director and the external auditor on the key accounting issues and areas of significant judgement.
- Confirmed the impact of new accounting standards IFRS15 (*Revenue from Contracts with Customers*) and IFRS9 (*Financial Instruments*).
- Reviewed a report from the Group finance department setting out the impact of IFRS16 (*Leases*) on the Group's financial statements, which will be implemented in the financial year beginning 1 October 2019.
- Reviewed the trading updates at meetings held in January, March and August.
- Reviewed the effectiveness of the Group's internal control and risk management procedures and, where appropriate, made recommendations to the Board on areas for improvement.
- Invited the Director of Internal Audit to attend meetings to review the results of the Internal Audit work for the current year and to agree the scope and focus of Internal Audit work to be carried out in the following year.
- Received reports on developments in relation to the Competition and Markets Authority market study of the statutory audit market; the Brydon Review (set up to examine the quality and effectiveness of audit); Kingman Review into the Financial Reporting Council ("FRC") and the BEIS Select Committee report on the future of audit.
- Reviewed the UK Corporate Governance Code 2018 and future reporting under s172 Companies Act 2006.
- Approved the Committee work programme for 2019.
- Reviewed the whistleblowing arrangements and the use of a dedicated external independent and confidential telephone hotline service for all employees to raise concerns.

Audit Committee

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

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

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

The Audit Committee confirms that the Company has complied with the provisions of the Competition & Markets Authority Order throughout its financial year ended 30 September 2019 and up to the date of this report.

Engagement of the external auditor

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

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

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

During the year, the Committee carried out an assessment of the effectiveness of the external audit process for the previous year ended 30 September 2018. The assessment was led by the Chair of the Committee, assisted by the Group Finance Director and focused on certain criteria which the Committee considered to be important factors in demonstrating an effective audit process. These factors included the quality of audit staff, the planning and execution of the audit and the role of management in the audit process. This was the first year of PwC auditing the Group's financial statements and the assessment identified several matters that required improvement, principally caused by their unfamiliarity with the Group's businesses and their year end close process. The Committee was confident that PwC would address these matters during their 2019 audit.

The Committee also confirmed that none of these matters impacted on the quality or thoroughness of the audit and concluded that the external audit process remained effective and that it provides an appropriate independent challenge of the Group's senior management.

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

Non-audit services

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

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

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

Taxation services are not provided by the Group's current audit firm; a separate firm is retained to provide tax advice and any assistance with tax compliance matters generally. In addition, due diligence exercises on acquisitions and similar transactions are not provided by the auditor, but are placed with other firms. During the year, Deloitte LLP were appointed by the Company to carry out financial due diligence on VSP Technologies prior to the business being acquired by the Group in July 2019.

The Group auditor is retained to carry out assurance services to the Committee in connection with "agreed upon procedures" on the Group's Half Year consolidated financial statements. With the exception of this work, PwC has not provided any non-audit services to the Company or its subsidiaries and has confirmed their independence to the Audit Committee. The fees for carrying out this work comprises the total non-audit fees of £18,000 set out in note 27 to the consolidated financial statements.

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

Financial reporting and significant financial judgements

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

The Committee considered the matters set out below as being significant in the context of the consolidated financial statements for the year ended 30 September 2019. These were discussed and reviewed with management and the external auditor and the Committee challenged judgements and sought clarification where necessary. The Committee received a report from the external auditor on the work they had performed to arrive at their conclusions and discussed in detail all material findings contained within the report.

Accounting for acquisitions

The Committee reviewed the accounting for acquisitions completed during the year, in particular the acquisition of VSP Technologies for a consideration of £57.2m. The acquisition was material for the FY2019 audit and, in accordance with IFRS3 (*Business combinations*), management was required to include a fair value analysis of the acquisition accounting in this year's financial statements. The Committee agreed that the external auditor carry out an audit of a) the Purchase Price Allocation ("PPA") prepared by the Group finance department; b) substantive detailed testing of the opening balance sheet as at the acquisition date; c) audit of any fair value adjustments arising on the acquisition balance sheet; and d) testing procedures over the closing balance sheet. The Committee, in light of the audit testing concluded that the accounting for this acquisition and three smaller acquisitions was appropriate.

Provisions for excess and slow moving inventory

The Committee reviewed the Report of the Group Finance Director that set out the gross balances by business, together with any related provision against the carrying value. The Committee reviewed the bases used to value and confirm existence of inventory held across the Group; they also considered the appropriateness of provisions held against the carrying value of inventory, having regard to the age and volumes of inventory, relative to expected usage.

Following their review, which also included consideration of the external audit findings, the Committee concluded that the provision for excess and slow moving inventory is appropriate.

Impairment of goodwill

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

In addition to the above, the Committee also seeks confirmation from the auditor that the Group's businesses follow appropriate policies to recognise material streams of revenue and their audit work carried out more generally has assessed any instances where management may be able to override key internal controls designed to guard against fraud or material misstatement.

The auditor also reported to the Committee on other less material matters including the recoverability of trade receivables, accounting for tax and the valuation of the Group's defined benefit pension schemes.

In May 2019, the Company received a letter from the Corporate Reporting Review Team ("CRRT") of the FRC in relation to its formal review and assessment of the quality of corporate reporting in the UK. The CRRT reported that they had no matters which required a response following their review of the Group's Annual Report & Accounts for the year ended 30 September 2018.

Changes in accounting standards

The Audit Committee reviewed the likely impact of adopting IFRS16 (*Leases*) ahead of the implementation across the Group, which will be applicable for the year ending 30 September 2020. A report prepared by the Group Finance department on the potential impact of this standard on the Group's consolidated financial statements was submitted to the Committee. This report was based on a detailed review carried out in conjunction with the Heads of Finance of the major businesses. The Committee reviewed and challenged management's key judgements in assessing the impact on the financial statements. Further information on the impact of IFRS16 is set out in the Group's accounting policy on pages 87 and 88.

Tax strategy

The Committee meets annually with the Head of Tax and Treasury to review the key tax matters affecting the Group and to understand the areas of tax focus in the forthcoming year. This year the Committee reviewed a report on the potential impact that new legislation on Corporate Criminal Facilitation of Tax Evasion would have on the Group.

The Committee approved a Group policy including training, designed to ensure that all of the businesses complied with this new legislation. The Committee also confirmed that the Group's tax strategy and broader tax policy would be reviewed again in 2020, having been approved in 2018.

Risk management and internal control

The principal risks and uncertainties that are currently judged to have the most significant impact on the Group's long term performance are set out in a separate section of the Strategic Report on Internal Control and Risk Management on pages 28 to 31.

The Committee is responsible for reviewing the effectiveness of the Group's system of internal control. The system of internal control is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement or loss. The Group has the necessary procedures in place to ensure that there is an ongoing process for identifying, evaluating and managing the principal risks to the Group. These procedures are in line with the FRC's guidance.

Audit Committee Report continued

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

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

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

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

The Committee has reviewed the effectiveness of the Group's risk management and internal control systems for the period from 1 October 2018 to the date of this Report. Taking into account the matters set out on pages 28 to 31 relating to principal risks and uncertainties and the reports from the Director of Internal Audit, the Board, with the advice of the Committee, is satisfied that the Group has in place effective risk management and internal control systems.

Internal Audit

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

Following the difficulties that arose on implementation of the new ERP system in the US Industrial Seals business earlier in the year, the Group Director of Internal Audit was asked to undertake a detailed review of the implementation process. Following this initial review, he was seconded to the business to assist with resolving the ERP issues and in September was appointed VP Finance of the US Industrial Seals business.

The Group Senior Internal Auditor has been promoted to Group Internal Audit Director and a new Internal Auditor will shortly join the department.

A full programme of Internal Audit visits has been completed during the year. The scope of work carried out by Internal Audit generally focuses on the internal financial controls and risk management procedures operating within each business, including regulatory and compliance reviews and business process improvements. In January, the Group Director of Internal Audit presented his audit plan for the year to the Committee for their approval. Formal written reports are prepared on the results of each Internal Audit visit that set out internal control

weaknesses/risks identified during their work, together with recommendations to improve the internal control environment and mitigate these weaknesses/risks. These reports are discussed with management of the business visited and are reviewed by the appropriate member of the EMC.

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

There were no significant or high risk matters identified in the internal audits undertaken during the current financial year. Several recommendations were again made this year to the businesses in regards to implementing adequate and effective internal controls and procedures aimed at improving the quality and formality of the existing inventory cycle count procedures at various businesses. The Group Director of Internal Audit also reported that good progress has been made with addressing those recommendations made in 2018 related mainly to strengthening cybersecurity controls across all businesses and on improving user access controls within existing ERP systems.

The work of the Internal Audit department included a review of progress made by Group businesses in ensuring that their internal control environment was sufficiently robust to resist cyber-attacks and to confirm that all businesses have obtained the Cyber-Essentials Basic certification.

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

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

Sanctions

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

Anti-bribery and corruption

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

Whistleblowing

The Committee also monitors the Group's whistleblowing policy, which provides the framework to encourage and give employees confidence to "blow the whistle" and report irregularities. The policy, together with hotline posters are placed on site noticeboards across the Group. Employees are encouraged to raise concerns via the confidential multilingual hotline, which is managed by an independent external company and is available 24/7, 365 days a year. Reports to the hotline are investigated and reported to the Committee, together with details of corrective action taken. The Group received five such whistleblowing reports during the year, four of which on further investigation were found to be personal grievance matters. All cases reported to the Committee were satisfactorily resolved.

Nomination Committee Report

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

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

The Group Company Secretary acts as Secretary to the Committee.

Appointment of Chief Executive Officer ("CEO")

After a short period as Group CEO, Richard Ingram stepped down as CEO and Executive Director on 28 August 2018 and left the Company. John Nicholas was appointed as interim Executive Chairman by the Board during the interregnum period from 26 August 2018 until the appointment of Johnny Thomson as Group CEO on 25 February 2019.

Following Richard Ingram's departure, the Nomination Committee commenced a new process to find a permanent replacement CEO and Korn Ferry, a search consultancy, was appointed to assist with the process. Korn Ferry had not provided any other services to and had no other connection with the Company. The Committee followed a similar appointment process as adopted in 2017, amended to reflect specific lessons learned from the earlier recruitment process.

This updated process comprised:

- a detailed specification for the role was prepared against which potential candidates were considered;
- Korn Ferry provided a longlist of potential candidates to the Committee in September 2018;
- a shortlist of candidates was then selected based on both their desire to be considered for the role and on the Committee's assessment of their career background and experience;
- after an initial interview with the Chairman, four preferred candidates were selected by the Committee to go forward for formal interview;
- the interview process was led by the Chairman and Senior Independent Director;
- the candidates were also interviewed by the other non-Executive Directors and by the Group Finance Director;
- character references and psychometric tests were also undertaken on each candidate;
- a preferred candidate recommendation was made by the Committee in December 2018; and
- a sub-Committee met with the preferred candidate, to negotiate a remuneration package within the Directors' Remuneration Policy and the range recommended by the Remuneration Committee. The Committee subsequently made a recommendation to the Board to appoint Johnny Thomson, which the Board approved. Johnny Thomson joined the Board as CEO on 25 February 2019.

Retirement of the Group Finance Director

On 8 October 2019, Nigel Lingwood informed the Board of his intention to retire as Group Finance Director of Diploma PLC before the end of September 2020 and to terminate his employment with the Company with effect from 7 October 2020.

The Committee has delegated the recruitment process for the new Group Finance Director to Johnny Thomson, Group CEO with support from Jill Tennant, Group HR Director.

After appropriate consideration and review, Johnny Thomson recommended and the Committee concurred that the Inzito Partnership ("Inzito") be retained as the search consultancy to lead the process. Inzito does not provide any other services to, or have any connection with the Company.

Johnny Thomson and Jill Tennant have worked with Inzito to put together a comprehensive role brief and candidate specification, with input from Committee members. Careful consideration has been given to the background, skills, knowledge and experiences that will

be required of the Company's Group Finance Director in the future, taking into account the challenges and opportunities facing the Company. The search is in an early stage at the date of this Report, but a list of candidates is being prepared and will shortly be provided to the Committee. Before any appointment is made by the Board, the Committee will ensure the appointment meets the requirements laid out in its Terms of Reference. Further details of the process will be set out in the 2020 Annual Report & Accounts.

Succession planning

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

In January each year, the Committee also reviews succession planning risks and opportunities in relation to the Company's senior executives, which comprise a cadre of ca. 110 senior managers across the Group's businesses.

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

As part of the review of the composition of the Board and the succession planning process set out above, both the Board and the Committee recognise the importance of pursuing opportunities for both gender and ethnic diversity throughout the Group. The Board's commitment to gender and ethnic diversity is set out on page 38.

Non-Executive tenure as at 30 September 2019 (years served)



Committee evaluation

As explained on page 39, an internal evaluation of the performance of the Committee and its members was undertaken during the year and the evaluation confirmed that the Committee was operating effectively.

KEY DUTIES AND FOCUS IN 2019

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

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

The Committee's key focus areas during the year have been the CEO succession, recruitment of an additional non-Executive Director, leadership development and senior management succession planning. At the year end the Committee's focus is on recruiting an additional non-Executive Director and overseeing the recruitment of a new Group Finance Director.

Remuneration Committee Report



Our approach to remuneration is aligned to Diploma's strategy and promotes long term value creation. Our new Remuneration Policy supports individual and corporate performance. We are developing our governance in response to the evolving market expectations."

Andy Smith

Chairman of the
Remuneration Committee



Members of Committee	Attendance
Andy Smith (Chairman)	11/11
Anne Thorburn	11/11
John Nicholas (from 25 February 2019)	4/4
Charles Packshaw	11/11

Dear Shareholder

The management and their teams have, once again, delivered excellent results demonstrating continuing strong alignment between performance delivery and reward.

In light of the significant business growth in recent years (12% p.a. revenue growth over the five years to September 2019 and a 43% increase in market capitalisation since the Remuneration Policy ("the Policy") was last approved), the appointment of our new CEO in 2019, the upcoming need to recruit a new Group Finance Director following the announcement of Nigel Lingwood's retirement, recent developments in market practice and shareholder expectations, the Committee has decided to review the Policy in full a year early to ensure that it remains appropriate for the business at this time. We will therefore be putting a revised Policy up for approval at the 2019 AGM on 15 January 2020. Diploma has performed consistently well over many years and it was in 2014, when the market capitalisation of the Company was ca. £800m, that we last made changes to our total compensation parameters. The fundamentals of Diploma's successful remuneration practice will remain: a simple design to align executive and shareholder reward a strong and transparent link between performance and reward; and stretching performance targets on key metrics. The changes are set out in the Policy Change Table on page 48.

To further align with the business's strategy and drive value creation, we have reviewed our measures for the annual bonus and the long term incentive plan ("PSP"). For FY2020, we will diversify the annual bonus measures moving from 100% based on adjusted operating profit to 50% adjusted operating profit, 25% revenue and 25% free cash flow. Threshold will be triggered by minus 5% on budget, target will be budget and maximum will be plus 5% on budget. For the PSP we are maintaining 50% adjusted EPS and 50% TSR, but we are adding a ROATCE underpin to the adjusted EPS element.

For 2019, I am delighted to confirm an annual bonus payout of 72% of maximum and that the PSP awards granted in 2016 have vested at the maximum. Full details are set out on page 56 of the Annual Report & Accounts. Base salaries for the new financial year (that is, from 1 October 2019) will increase by 3.0% (2018: 3.0%) for Executive Directors. This reflects general pay inflation in the geographies the Company operates in and compares to the average increase of 4% across the senior management cadre.

We welcomed Johnny Thomson as CEO in February 2019. The demand for candidates of his calibre is high and to attract him it was necessary to award a higher salary than his predecessor and to offer an increased PSP opportunity of 250% of salary for each of his first three years. The Committee applied discretion to provide a full year annual bonus opportunity, and 2019 and 2020 PSP grants at the exceptional level of 250% of salary. Importantly, the Company made no payments to "buyout" or compensate Johnny for any bonuses foregone or long term incentive awards that lapsed when he left his previous employer. His compensation package is less than he earned at his previous employer and his total target remuneration is around 10% above the median compared to FTSE-listed companies of a similar size.

In October 2019, Nigel Lingwood, Group Finance Director, gave notice of his intention to retire in October 2020. We are extremely grateful for Nigel's contribution over the years and in particular, during the recent CEO transitional period and our intention is to treat Nigel as a good leaver.

Executive remuneration continues to attract much attention, analysis and debate. I am pleased that the fundamental relationship between pay and performance remains strong at Diploma. The revised Policy will ensure this continues whilst enabling Diploma to attract, retain and motivate the talent it needs as it continues its impressive growth record.

I look forward to meeting shareholders at this year's AGM on 15 January 2020 and will be pleased to answer any questions on the Company's remuneration policies.

Andy Smith
18 November 2019

Remuneration Committee

The Remuneration Committee ("the Committee") is chaired by Andy Smith and comprises independent non-Executive Directors. John Nicholas re-joined the Committee on 25 February 2019 on stepping down as interim Executive Chairman, following the appointment of Johnny Thomson as Group CEO.

The Chief Executive Officer/Executive Chairman (whilst in place) and the Group HR Director attend meetings at the invitation of the Committee to provide advice to help it make informed decisions. The Group Company Secretary attends meetings as Secretary to the Committee.

The Remuneration Committee Report

The Report has again been presented this year in two sections. The first section sets out the Directors' Remuneration Policy ("the Policy"), and the second section of this Report sets out the annual remuneration paid to the Directors in the year ended 30 September 2019 in accordance with the existing Remuneration Policy approved on 17 January 2018. The proposed new Policy will be subject to approval by the shareholders at the AGM on 15 January 2020; the second section of the Report will be subject to an advisory vote by the shareholders at the AGM.

The Committee has reviewed each element of the Policy in detail, taking advice on best practice and market expectations from our independent advisors. We have concluded that, while the broad structure of the Policy remains appropriate for Diploma, there are a number of areas where we are proposing amendments such that the Policy better supports the interests of the Company and its stakeholders.

Remuneration principles and structure

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

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

These principles align to those of the wider workforce.

The Policy Table on pages 48 and 49 summarises the components of reward for the Executive Directors of Diploma PLC that will govern the Company's intentions as regards future payments. More detailed descriptions of the incentive plans are given in the following sections.

Policy Changes

We have consulted with our largest twenty shareholders who hold over 60% of shares and the key proxy voting agencies. We also considered the best-practice features set out in the FRC's 2018 UK Corporate Governance Code. In finalising our policy, we have amended our approach in response to the feedback. The principal proposed changes to the policy are as follows and are summarised in the Policy Change Table on page 48:

Performance related remuneration – we want to strengthen the alignment of interests between shareholders and management by increasing our longer-term share-based incentives. The maximum PSP award for CEO will increase to 250% of salary and for other Executive Directors to 200% of salary. The maximum annual bonus opportunity will remain at 125% of salary for the CEO and increase to 125% of salary (from 100%) for other Executive Directors. This results in a long-term opportunity positioned at the upper quartile for companies of a similar size, balanced by annual bonus opportunity at the lower quartile.

Minimum shareholding requirement – will increase to 250% of base salary for the CEO and remain at 200% for other Executive Directors.

Malus and clawback – we have introduced an additional trigger relating to corporate failure to provide additional protection for the Company and shareholders.

Post cessation shareholding requirement – a two-year holding period is already in place for vested PSP awards. In addition, the CEO will be required to hold shares to the value of 125% of salary and other Executive Directors in value of 100% of salary for 12 months after they leave the Company.

Pensions – we acknowledge that historic pension practices for Executive Directors no longer accord with the developing environment and we are evolving our approach accordingly. The Company pension contribution for any new hires will be set at the same level as the majority of our UK workforce, presently 4% of salary. Johnny Thomson was recruited with a pension contribution of 15% which was a reduction from previous practice and comparable to other senior management in Diploma. Management will review the pension provision for the UK workforce over the coming year. This will form the basis for the design of a transition plan for existing employees which takes into account the contractual commitments we have made. Pending the output of this work, Johnny will take a reduction in his pension contribution from 1 October 2020, as a step towards aligning with the UK workforce.

Performance Share Plan ("PSP") – this is due to expire in 2021. The Committee has reviewed the relevant documentation and, as applicable, incorporated the changes outlined above and is requesting shareholder approval to adopt the PSP. We will seek approval for a new set of PSP rules at the AGM on 15 January 2020, which will have a life of ten years.

KEY DUTIES AND FOCUS IN 2019

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

The Committee's roles and responsibilities are set out in its Terms of References, which are reviewed annually and approved by the Board. The Terms of Reference are available on Diploma PLC's website at www.diplomapl.com/governance/constitutional-documents.

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

- Approved Remuneration Committee work programme for 2019.
- Reviewed the AGM 2019 votes on the 2018 Remuneration Committee Report.
- Approved the Director's service contract for the new CEO.
- Approved proposed retirement arrangements for Nigel Lingwood.
- Approved annual performance bonus targets and the subsequent bonus awards for 2019.
- Approved new PSP awards to Executive Directors and confirmed the performance conditions for such awards.
- Confirmed the vesting percentages for the PSP awards made in December 2016 which crystallised in 2019.
- Reviewed and proposed the new Directors' Remuneration Policy.
- Reviewed the rules of the Diploma PLC 2011 Performance Share Plan and recommended its renewal.
- Reviewed Executive Directors' salaries, pensions and benefits.
- Reviewed the fees of the Chairman and non-Executive Directors.
- Reviewed remuneration of senior management in the operating businesses.
- Approved the 2019 Remuneration Committee Report.

Remuneration Committee Report continued

DIRECTORS' REMUNERATION POLICY

The Policy Change Table

The Table below summarises the key Policy changes:

Policy element	Changes proposed (2020)
Pension	<ul style="list-style-type: none"> Pension contributions for existing Executive Directors will be no higher than 15%¹. Pension contributions for new Executive Director appointments will be no higher than the rate offered to the majority of our UK workforce, which is currently 4% of salary.
Annual bonus	<ul style="list-style-type: none"> Maximum opportunity of 125% of salary for all Executive Directors.
Long term incentive plan – PSP Award	<ul style="list-style-type: none"> Maximum opportunity of 250% of salary for CEO, maximum opportunity of 200% for other Executive Directors.
Share ownership requirement	<ul style="list-style-type: none"> Amend from “guideline” to “requirement” To ensure alignment with the interests of our shareholders, the requirement for the CEO to be increased to 250% of salary.
Malus and clawback	<ul style="list-style-type: none"> As proposed by the Corporate Governance Code, introduction of an additional trigger relating to corporate failure.
Post-cessation shareholding requirements	<ul style="list-style-type: none"> The CEO will continue to be required to hold shares in value of 125% of salary and other Executive Directors in value of 100% of salary for twelve months after their termination date (or if less, the value of shares held at the date of cessation that will count for this requirement). Post cessation shareholding requirements will apply to shares which have been granted under the Company's Performance Share Plan after the approval of the Policy.

The Remuneration Policy Table

The Remuneration Policy Table set out below summarises the components of reward for the Executive Directors of Diploma PLC that will govern the Company's intentions as regards future payments of remuneration.

This Policy, if approved by shareholders at the AGM on 15 January 2020, will apply from that date for a term of three years unless another Policy is approved by shareholders at an earlier date. Any commitment made by the Company prior to the approval and implementation of the Policy set out in the Report which was consistent with the Policy in force at the time, can be honoured, even if it would not be consistent with the Policy prevailing when the commitment is fulfilled.

Executive Directors

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Base salary	To attract and retain people of the calibre and experience needed to develop and execute the Company's strategy.	Salaries are reviewed annually, with changes normally effective from 1 October.	<p>There is no maximum limit set. Salaries will be market competitive to retain skilled executive talent and attract new talent as required.</p> <p>Salary increases will generally be no higher than those awarded to other employees, although the Committee retains discretion to award larger increases if it considers it appropriate.</p>	Salary levels and increases are determined based on a number of factors, including individual and business performance, level of experience, scope of responsibility, salary increases both for UK employees and for the senior management cadre more generally and the competitiveness of total remuneration against companies of a similar size and complexity.
Pensions	Designed to be fair within the market to reward sustained contribution by Executive Directors.	Pension contributions can either be paid directly into a personal pension savings scheme or taken as a separate cash allowance.	<p>For current Executive Directors pension contributions of up to 15% of salary.¹</p> <p>Pension contributions for new Executive Director appointments will be no higher than the rate offered to the majority of our UK workforce, which is currently 4% of salary.</p>	No performance metric.
Benefits	To provide a competitive package of benefits.	Includes various cash/non-cash benefits such as: payment in lieu of a company car, life assurance, income protection, annual leave, medical insurance. The Committee may offer any additional benefits it considers appropriate in line with the interests of the Company and local market practice. Any renewable business related expenses (including tax thereon) can be reimbursed if determined to be a taxable benefit.	No maximum limit is prescribed, but the Committee monitors annually the overall cost of the benefit provision.	No performance metric.

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Annual Performance Bonus Plan	To incentivise and reward Executive Directors on the achievement of the annual budget and other business priorities for the financial year.	<p>Provides an opportunity for additional reward based on annual performance against targets set and assessed by the Committee.</p> <p>Where shareholding guidelines have not been met, half of any annual bonus awarded (net of tax) will be deferred in shares, but will remain eligible for dividends. The remaining bonus shall be paid in cash following the relevant year end.</p> <p>Malus and clawback provisions apply to bonus awards.</p> <p>The Committee may amend the formulaic outcome should it not be a fair reflection of the Company's underlying performance or in exceptional circumstances.</p>	<p>Maximum of 125% of base salary for the Executive Directors.</p> <p>Performance below threshold results in zero payment. On-target bonus is 50% of maximum bonus and threshold performance is 5% of base salary.</p>	<p>Performance metrics are selected annually based on the current business objectives. The majority of the bonus will be linked to financial performance.</p> <p>Different performance measures, including personal objectives, may be used for future cycles to take into account changes in the business strategy. Personal objectives, if used, will account for no more than 20% of the bonus.</p>
Long Term Incentive Plan – PSP Award	Incentivise Executive Directors to achieve superior returns and long term value growth.	<p>Performance assessed over rolling three-year performance periods.</p> <p>Awards are discretionary and do not vest until the date on which the performance conditions are determined. If employment ceases during a three-year performance period, other than in the case of a "good leaver", awards will normally lapse.</p> <p>The Committee expects that typically awards of 250% will be made to the CEO, and awards of up to 200% will be made to the other Executive Directors.</p> <p>For awards granted after 17 January 2018, Executive Directors will be required to retain shares vesting under the LTIP (net of tax) until the fifth anniversary of grant.</p> <p>Awards may include dividend equivalents which are cash bonuses or shares in lieu of dividends foregone on vested shares, from the time of award up to the time of vesting.</p> <p>Malus and clawback provisions apply.</p> <p>The Committee may amend the formulaic outcome should it not be a fair reflection of the Company's underlying performance or in exceptional circumstances.</p>	<p>The maximum opportunity as a percentage of salary is 250% for the CEO and 200% for other Executive Directors for each award made under the 2020 PSP.</p> <p>No more than 25% of the award will be payable at threshold performance.</p>	<p>Awards will be granted subject to a combination of financial measures (including, for example, adjusted EPS, ROATCE and TSR), tested over a period of at least three years.</p> <p>The Committee may change the weighting of the performance measures or introduce new performance measures for future awards, so that they are aligned with the Company's strategic objectives.</p>

Chairman and non-Executive Directors

Component	Purpose and link to strategy	Operation	Maximum opportunity	Performance metrics
Chairman and non-Executive Directors' fees	To attract and retain a Chairman and independent non-Executive Directors of the required calibre and experience.	<p>Paid quarterly in arrears and reviewed each year.</p> <p>Any reasonable business related expenses (including tax thereon) if determined to be a taxable benefit can be reimbursed.</p>	The Chairman's and non-Executive Directors' fees are determined by reference to the time commitment and relevant benchmark market data.	Annual Board evaluation.

¹ Nigel Lingwood, Group Finance Director, receives a contribution of 20%. Nigel Lingwood has given notice of his intention to retire by 7 October 2020. There will be no change to Nigel Lingwood's contribution and his successor will be appointed under the new Policy.

Remuneration Committee Report continued

DIRECTORS' REMUNERATION POLICY CONTINUED

Pay-for-performance: Executive Director's potential value of 2020 remuneration package

Johnny Thomson (%)

Minimum	87	13	£818,000		
Target	34	5	20	41	£2,112,000
Maximum	21	3	25	51	£3,405,000
Stretch	17	2	20	61	£4,268,000

Fixed: ● Base salary and benefits ● Pension

Variable: ● Annual performance bonus ● Long term incentive plans

1 Base salary is as at 1 October 2019; benefits are as set out on page 54.

2 Stretch is calculated on the same basis as the Maximum bar, however, it includes a share price uplift of 50% over three years for the PSP.

Nigel Lingwood (%)

Minimum	84	16	£429,000		
Target	38	7	23	32	£943,000
Maximum	25	5	29	41	£1,457,000
Stretch	21	4	24	51	£1,757,000

On-target remuneration assumes an Annual Performance Bonus Plan of 50% of the maximum for the Executive Directors. It has been assumed that a face value limit of 250% of base salary (Group Finance Director: 175%) applies to each PSP award. On target vesting of PSP awards assumes an adjusted EPS growth of 8% p.a. and TSR performance which is equivalent to 50% of the maximum vesting under the PSP. Maximum remuneration assumes maximum annual performance bonus and maximum vesting of PSP awards. No share price growth or dividend equivalents are assumed, other than in the Stretch bar.

Executive Directors

Base salary

Salary levels are determined based on a number of factors, including individual calibre and experience, their latest pay package, scope of responsibility and competitiveness of total remuneration against companies of a similar size and complexity.

In determining the annual base salary increases which apply from 1 October, the Committee considers a number of factors, including individual and business performance, scope of responsibility, comparative salaries in companies of a similar size and complexity and the range of remuneration increases applying across the Group.

The Committee also takes into account the salary increases applying across the senior management cadre. This comparator group comprises ca. 110 senior managers across the Group's businesses. This senior management cadre has been chosen as a representative group, as it provides a meaningful comparison considering the global and diverse nature of the Group's business.

Annual performance bonus

The Diploma PLC Annual Performance Bonus Plan is substantially a cash-based scheme designed to reward the Executive Directors for meeting stretching annual performance targets. The level of bonus payable for achieving the minimum target is 5% of base salary. No bonus is payable if performance does not meet the minimum target.

At the start of the financial year the Committee agrees the performance measures for the Annual Performance Bonus Plan for the year ahead based on agreed financial targets for the business.

The 2020 Annual Performance Bonus Plan sees a diversification of performance measures from 2019 to better align with the Company's objectives under Johnny Thomson's leadership as CEO. Group adjusted operating profit at constant currency remains the key deliverable and will account for 50% of the bonus. In addition, there will be two additional measures: 25% of the bonus will be based on revenue performance at constant currency and 25% will be based on free cash flow. Threshold will be reached at minus 5% on budget, on-target will be budget and maximum will be plus 5% on budget.

As part of the new Policy, the Committee has discretion to override formulaic outcomes and amend payouts under the Annual Bonus Plan, should it determine that either it is not a fair reflection of the underlying performance of the business over the relevant performance period or in exceptional circumstances.

The definition of adjusted operating profit is consistent with the Group's financial statements (see note 2 to the consolidated financial statements). However, the Committee has discretion to make amendments to take account of changes in accounting policy and/or material operational, market, exchange rate or environmental factors in order to more appropriately reflect management performance.

At the end of the financial year, the Committee meets to assess the performance of each Executive Director against the financial and individual objectives. Bonuses are normally paid in cash in December. The Policy requires that 50% of any bonus awarded for the financial year ending 30 September 2019, or thereafter, is deferred on a net of tax basis into shares until minimum shareholding requirement levels have been met. Minimum shareholding requirements have been increased for the CEO to ensure alignment with the interests of shareholders.

Long term incentive award

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

This PSP will expire in 2021. To maintain alignment with the Policy the Committee has reviewed the PSP one year ahead of its expiry. We are therefore asking shareholders to approve a new PSP, based on the existing PSP but updated to reflect changes in policy and best practice developments at the 2020 AGM (2020 PSP).

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

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

The face value of an award is equal to the number of shares, or shares under option, multiplied by the relevant share price. The relevant share price will be the mid-market closing share price on the dealing day before the award. Normal awards are expected to be at 250% of salary for the CEO and up to 200% of salary for other Executive Directors.

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

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

The Committee believes that these continue to be the right measures to assess the delivery of the Board's updated strategy. Reflecting the importance of ROATCE, the Company has introduced a ROATCE underpin on the adjusted EPS element which will ensure adjusted EPS growth is in the best interests of shareholders. This will be measured as the reported ROATCE against an agreed target in the third year of the performance condition.

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

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

As part of the new Policy the Committee has discretion to override formulaic outcomes and amend payments under the PSP, should it determine it is either not a fair reflection of the underlying performance of the business over the relevant performance period, or in exceptional circumstances.

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

For awards granted after 17 January 2018, Executive Directors are required to retain shares vesting under the PSP (net of tax) until the fifth anniversary of grant ("the Holding Period"), in order to provide longer term shareholder alignment. The Holding Period continues to apply to post cessation of employment and shall expire on the earliest of:

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

Service contracts

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

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

The Executive Directors' service contracts, copies of which are held at the Company's registered office, together with any service contract for new appointments, contain provisions for compensation in the event of early termination or change of control, equal to the value of salary and contractual benefits for the Director's notice period. The Company may make a payment in lieu of notice in the event of early termination and the Company may make any such payment in instalments with the Director being obliged in appropriate circumstances to mitigate loss (for example by gaining new employment).

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

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

	Contract date	Unexpired term	Notice period	Compensation payable upon early termination
Johnny Thomson	15 Jan 2019	Rolling	1 year	1 year
Nigel Lingwood ¹	20 Mar 2014	Rolling	1 year	1 year
John Nicholas ²	2 Oct 2018	-	1 month	1 month

¹ Nigel Lingwood has informed the Board that he plans to retire as Group Finance Director and he has given notice in accordance with the terms of his Service Contract.

² John Nicholas stood down as interim Executive Chairman following the appointment of Johnny Thomson as CEO on 25 February 2019.

Other remuneration policies

Payment for loss of office

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

Remuneration Committee Report continued

DIRECTORS' REMUNERATION POLICY CONTINUED

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

- Notice period of 12 months' base salary, pension and contractual benefits or payment in lieu of notice.
- Bonus payable for the period worked, subject to achievement of the relevant performance condition. Different performance measures (to the other Executive Directors) may be set for a departing Director as appropriate, to reflect any change in responsibility.
- Vesting of award shares under the Company's long term incentive plan is not automatic and the Committee would retain discretion to allow partial vesting depending on the extent to which performance conditions had been met and the length of time the awards have been held. Time pro-rating may be disappplied if the Committee considers it appropriate, given the circumstances. For awards granted prior to 17 January 2018, performance will be measured to the date of cessation of employment and, to the extent applicable, vest shortly thereafter. For awards granted after 17 January 2018, performance will be normally measured to the end of the normal performance period and, to the extent applicable, vest on the normal vesting date, save in exceptional circumstances when the Committee may determine that early vesting should still apply.
- The Committee will provide for the leaver to be reimbursed for a reasonable level of legal fees in connection with a settlement agreement and outplacement services, where appropriate.

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

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

Change of control

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

Malus and clawback

Malus provisions apply to all awards made under the Company's long term incentive and annual bonus plans which give the Committee the right to cancel or reduce unvested share awards (or in the case of the Annual Performance Bonus Plan, cash payments) in the event of material misstatement of the Company's financial results, miscalculation of a participant's entitlement, individual gross misconduct or of corporate failure (resulting in a liquidation or the appointment of administrators). Corporate failure is an addition from this policy review.

The clawback arrangements permit the Committee to recover amounts paid to Executive Directors in specified circumstances and further safeguard shareholders' interests.

Remuneration for new appointments

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

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

- The remuneration structure will be kept simple where practicable, hence the use of base salary, benefits, pension (or cash allowance in lieu), annual performance bonus and long term incentives.
- The emphasis on linking pay with performance shall continue; hence the use of variable pay in the form of an annual performance bonus and a long term incentive award, which will continue to be a significant component of the Executive Directors' total remuneration package.
- Initial base salary will take into account the experience and calibre of the individual and their existing remuneration package. Where it is appropriate to offer a lower salary initially, a series of increases to the desired salary positioning may be given over subsequent years subject to individual performance.
- The structure of variable pay will be in accordance with Diploma's approved Policy detailed above with a maximum aggregate variable pay opportunity of 375% of salary for the CEO and 325% for other Executive Directors. Different performance measures may be set in the first year for the annual bonus, taking account of the responsibilities of the individual and the point in the financial year that the executive joined the Company.
- Benefits will generally be provided in accordance with the approved Policy, with relocation expenses/an expatriate allowance paid, if appropriate.
- In the case of an external recruitment, the Committee may also offer additional cash and/or share-based elements when it considers these to be in the best interests of Diploma and shareholders, to replace variable remuneration awards or arrangements that an individual has foregone in order to join the Group. This includes the use of awards made under section 9.4.2 of the UK Listing Rules. Any such payments would take account of the details of the remuneration foregone including the nature, vesting dates and any performance requirements attached to that remuneration and any payments would not exceed the expected value being forfeited.
- In the case of an internal appointment, any outstanding variable pay awarded in relation to the previous role will be allowed to pay out according to the terms of grant.
- For all new Executive Director appointments, the mandated shareholding requirement, deferral of annual performance bonus and the Holding Period for PSP awards will apply in accordance with the Policy and the relevant Plan rules.
- Fees for a new Chairman or non-Executive Director will be set in line with the approved Policy.

Committee discretion

The Committee operates the Annual Performance Bonus Plan and the Performance Share Plan ("the Plans") in accordance with the relevant Plan rules and where appropriate, the Listing Rules and HMRC legislation.

The Committee will exercise its powers in accordance with the terms of the relevant Plan rules. The Committee also has discretions to set components of remuneration within a range from time to time as set out in the maximum opportunity sections of the Policy Table.

The Committee retains discretion over a number of areas relating to the operation and administration of the Plans. These include but are not limited to:

- selecting the participants for the annual bonus and PSP awards;
- timing of awards and grants of setting performance criteria each year;
- determining the quantum of grants and/or payments (within the limits set out in the Policy Table);
- adjusting the constituents of the TSR comparator group;
- determining the extent of vesting based on the assessment of performance;
- to override formulaic outcomes and amend payouts under the Annual Bonus Plan and for PSP should it determine that either it is not a fair reflection of the underlying performance of the business or in exceptional circumstances;
- to apply or disapply time prorating;
- dealing with leavers;
- discretion to waive or shorten the Holding Period for shares acquired under the PSP;
- the discretion to retrospectively amend performance targets in exceptional circumstances, including making the appropriate adjustments required in certain circumstances (e.g. rights issues, corporate restructuring events, variation of capital and special dividends); and
- in respect of share awards, to adjust the number of shares subject to an award in the event of a variation in the share capital of the Company.

Dilution

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

Consultation with shareholders and employees

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

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

Policy in respect of external board appointments for Executive Directors

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

Employee and post-employment shareholding requirements

The Committee has adopted shareholding requirements for Executive Directors, to encourage substantial long term share ownership. Until the Policy review these have been "guidelines", whereas they are now "requirements". In addition, these requirements have been increased to ensure the stronger alignment of interests between Executive Directors and shareholders. These specify that, over a period of five years from the date of appointment, each Executive Director should build up and then retain a holding of shares with a value equivalent to 250% of base salary in the case of the CEO and for other Executive Directors, to 200% of base salary ("the MSR").

Vested PSP awards must be retained until the required shareholding level is reached.

As explained in the long term incentive award section on page 50, Executive Directors are required to hold shares vesting under the PSP (net of tax) until the fifth anniversary of the grant ("the Holding Period"). The Holding Period applies to post-cessation of employment except where cessation is by reason of death, if there is a change of control, or the Committee exercises its discretion.

In addition, a post-cessation shareholding requirement is being introduced of 50% of the MSR for 12 months after the termination date (or if less than the MSR, the value of shares held at the cessation date). Post-cessation holding will apply to shares which are granted under the PSP after the approval of the updated Policy.

As at 18 November 2019, the Group Finance Director exceeded the applicable shareholding requirements, while the CEO, having joined on 25 February 2019, has started to build his shareholding so as to meet the requirement within the five-year timescale.

Chairman and non-Executive Directors Recruitment and term

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

Chairman

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

Chairman and non-Executive Directors' letters of appointment:

	Date of original appointment	Date of re-election	Expiry of term
John Nicholas	1 Jun 13	16 Jan 19	20 Jan 21
Charles Packshaw	1 Jun 13	16 Jan 19	1 Jun 22
Andy Smith	9 Feb 15	16 Jan 19	9 Feb 21
Anne Thorburn	7 Sep 15	16 Jan 19	7 Sep 21

Fees

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

If there is a temporary yet material increase in the time commitments for non-Executive Directors, the Board may pay extra fees on a pro-rata basis to recognise the additional workload. In 2018, the Board approved additional fees to be payable to the Chairman, while he served as interim Executive Chairman up to 25 February 2019 when Johnny Thomson joined as CEO of the Company.

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

The following section of this Report provides details of the implementation of the existing Remuneration Policy for the Executive Directors for the years ended 30 September 2019 and 2018. All of the information set out in this section of the Report has been audited, unless indicated otherwise.

Remuneration Committee Report continued

ANNUAL REPORT ON REMUNERATION

The following section of this Report provides details of the implementation of the existing Remuneration Policy for the Executive Directors for the years ended 30 September 2019 and 2018. All of the information set out in this section of the Report has been audited, unless indicated otherwise.

Executive Directors

Total remuneration in 2019 and 2018

	Johnny Thomson ¹		Nigel Lingwood		John Nicholas ²	
	2019 £000	2018 £000	2019 £000	2018 £000	2019 £000	2018 £000
Salary	402	333	323	323	62	14
Benefits	14	18	18	18	-	-
Pension	60	67	65	65	-	-
Annual performance bonus	603	240	323	323	-	-
Short term remuneration (cash)	1,079	658	729	729	62	14
Long term incentive plans – dividend equivalent (cash)	-	39	46	46	-	-
Long term incentive plans – performance element	-	549	534	534	-	-
Long term incentive plans – share appreciation element	-	366	501	501	-	-
Long term share-based remuneration	-	915	1,035	1,035	-	-
Total	1,079	1,612	1,810	1,810	62	14

1 Johnny Thomson's salary, benefits and pension are for the period from joining the Company as CEO on 25 February 2019 to 30 September 2019. The annual bonus paid to Johnny Thomson, at the discretion of the Committee to facilitate recruitment, has not been time prorated.

2 John Nicholas was appointed interim Executive Chairman on 28 August 2018. The fees above relate to his executive service from 28 August 2018 to 25 February 2019; as interim Executive Chairman, John Nicholas was not entitled to benefits, pension, annual bonus or a long term incentive award. John Nicholas's fees for his role as non-Executive Chairman are set out on page 59.

The aggregate short term remuneration paid to Executive Directors in the year ended 30 September 2019 was £1.8m (2018: £2.0m).

Executive Director's other roles

John Nicholas is non-Executive Chairman of Porvair plc and received fees of £37,500 during his term as interim Executive Chairman of Diploma PLC.

Base salary

The average base salary increase for Executive Directors which applied from 1 October 2018 was 3.0%, compared with 4.5% for the Group's senior management cadre. On 12 November 2019, the Committee approved an increase of 3.0% in base salary for the CEO and the Group Finance Director which will apply in respect of the year commencing 1 October 2019.

Benefits

	2019				2018			
	Cash allowance in lieu of a car £000	Life assurance and income protection £000	Medical insurance £000	Total benefit £000	Cash allowance in lieu of a car £000	Life assurance and income protection £000	Medical insurance £000	Total benefit £000
Johnny Thomson ¹	9	4	1	14	-	-	-	-
Nigel Lingwood	11	6	1	18	11	6	1	18
John Nicholas ²	-	-	-	-	-	-	-	-

1 Johnny Thomson's benefits are for the period from 25 February 2019 to 30 September 2019.

2 John Nicholas was not entitled to benefits in his role as interim Executive Chairman which ended on 25 February 2019.

Pension

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

Pension contributions were applied as follows:

	2019				2018			
	Contribution rate % of base salary	Paid as cash allowance £000	Paid as pension contribution £000	Total cash paid £000	Paid as cash allowance £000	Paid as pension contribution £000	Total cash paid £000	
Johnny Thomson ¹	15	60	-	60	-	-	-	
Nigel Lingwood	20	67	-	67	65	-	65	
John Nicholas ²	-	-	-	-	-	-	-	

1 Johnny Thomson's pension contributions are for the period from 25 February 2019 to 30 September 2019.

2 John Nicholas was not entitled to a pension contribution in his role as interim Executive Chairman.

Annual performance bonus

The following table summarises the performance assessment by the Committee in respect of 2019 with regard to the Group financial objectives:

Performance measure	Targets for 2019	Overall assessment against targets
Adjusted operating profit (on a constant currency basis)	The minimum performance target of £84.9m was equal to the 2018 adjusted operating profit (as defined in note 2 to the consolidated financial statements) on a constant currency basis. The on-target performance was equal to £93.5m being the FY2019 budget (adjusted to FY2018 exchange rates). The maximum target was set at £97.6m representing 15% growth above the 2018 adjusted operating profit, on a constant currency basis.	Adjusted operating profit for 2019 was £97.2m which represented 12.2% growth on the 2018 adjusted operating profit on a constant currency basis. Minimum thresholds were exceeded for adjusted operating margins, free cash flow and ROATCE. 72.0% of the maximum award is payable.

Based on the performance set out above, the resulting bonus for each Executive Director relating to 2019 is as follows:

	2019 actual bonus – as a percentage of 2019 base salary					2019 bonus
	Minimum	On-target	Maximum	Financial objectives	Total bonus	£000
Johnny Thomson ¹	5%	63%	125%	90.0%	90.0%	603
Nigel Lingwood	5%	50%	100%	72.0%	72.0%	240
John Nicholas ²	–	–	–	–	–	–

¹ Johnny Thomson's bonus is for the full year and it has not been prorated for time served as Group CEO, following the application of discretion by the Committee. This decision was taken in order to facilitate the recruitment of Johnny Thomson, as explained by the Remuneration Committee Chairman in his letter at page 46. 50% of the bonus will be deferred into shares, on a net basis, until the minimum shareholding requirement has been met.

² John Nicholas was not entitled to a bonus in his role as interim Executive Chairman

In the financial year beginning 1 October 2019, the Annual Performance Bonus Plan will be based on the followings metrics: 50% will be based on adjusted operating profit, 25% will be based on revenue (both metrics measured on a constant currency basis) and the remaining 25% will be based on operating cash flow. The financial performance targets set for the Annual Performance Bonus Plan in 2019 will be disclosed in next year's Annual Report & Accounts.

Long term incentive awards

Performance conditions

Set out below is a summary of the performance conditions that apply to the PSP awards which vest in 2019 and the outstanding PSP awards, including those granted on 28 December 2017, on 7 December 2018 and on 25 February 2019 (for Johnny Thomson, on appointment as Group CEO). PSP awards have previously been granted at 175% of base salary. The Committee also exercised its discretion to grant Johnny Thomson an award of 250% of salary to facilitate his recruitment as Group CEO in February this year which was not prorated for time served. In determining the 2019 long term incentive award for Nigel Lingwood, the Committee considered the exceptional circumstances that prevailed whilst the Company worked through the recruitment, appointment and on-boarding of the new CEO in 2019. During this period, a significant additional load and responsibility fell to the Group Financial Director. The Committee believed that it was in shareholders' interests in these exceptional circumstances to grant him an award of 225% of salary.

The performance conditions apply to each award so that the vesting of 50% of the award is based on growth in adjusted EPS and 50% of the award is based on the relative TSR performance. The Committee has confirmed that the same performance conditions will be applied to PSP awards made in FY2020. In addition, in order for any payment to be earned under the EPS element of awards granted after 15 January 2020, the Committee must be comfortable that a satisfactory level of ROATCE performance has been achieved.

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

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

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

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

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

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

Remuneration Committee Report continued

ANNUAL REPORT ON REMUNERATION CONTINUED

Awards vesting in 2019

The PSP award made on 22 December 2016 to Nigel Lingwood, an Executive Director, was subject to operating performance conditions as set out in the table above, independently assessed over a three-year period ended 30 September 2019. The outcome of each award is shown in the table below:

Adjusted earnings per share:

	Base EPS	EPS at 30 Sep 2019	CAGR in EPS	Maximum target	Maximum award	Vested award
PSP (22 December 2016)	41.9p	64.3p	15.3%	14.0%	50%	50%

TSR growth against FTSE 250 (excluding Investment Trusts):

	TSR at 30 Sep 2019	Median	Maximum target	Maximum award	Vested award
PSP (22 December 2016)	24.0% p.a.	6.8% p.a.	15.2% p.a.	50%	50%

As a result of the above performance conditions, 100% of the shares awarded as nil cost options vested to Nigel Lingwood under the PSP award granted on 22 December 2016.

Set out below are the shares which vested to Nigel Lingwood at 30 September 2019 in respect of these awards.

	Share price at date of grant pence	Share price at 30 Sep 2019 pence	Proportion of award vesting	Shares vested number	Performance element ¹ £000	Share appreciation element ² £000	Total £000
Nigel Lingwood – PSP	997.5p	1,663p	100%	55,035	549	366	915

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

2 The share appreciation element represents the additional value generated through appreciation of the share price from the date the awards were granted to the end of the three-year performance period on 30 September 2019.

Dividend equivalent payments

Dividend equivalent payments of £38,965 (2018: £46,102) are payable to Nigel Lingwood in respect of awards which vested on 30 September 2019. These payments are included in this year's Annual Report on Remuneration.

Long term incentive plan – awards granted in the year

Nigel Lingwood and Johnny Thomson received grants of PSP awards on 7 December 2018 and on 25 February 2019, respectively, in the form of nil-cost options. These awards were based on a share price of 1,209p (Nigel Lingwood) and 1,364p (Johnny Thomson), being the mid-market price of an ordinary share in the Company at close of business on the day immediately preceding the award.

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

The performance conditions for these awards are set out on page 55.

Outstanding share-based performance awards

Set out below is a summary of the share-based awards outstanding at 30 September 2019, including both share awards which have vested during the year (based on performance) and share awards which have been granted during the year. The awards set out below were granted based on a face value limit of 175% of base salary for each award granted in prior years. In FY2019 awards were granted at 225% to Nigel Lingwood and at 250% to Johnny Thomson, as explained on page 55. No awards will vest unless the performance conditions set out on page 55 are satisfied.

Diploma PLC 2011 Performance Share Plan

	Market price at date of award	Face value of the award at date of grant £000	End of performance period	Vesting date	Shares over which awards held at 1 Oct 2018	Shares over which awards granted during the year	Vested during the period	Lapsed during the period	Shares over which awards held at 30 Sep 2019
Johnny Thomson¹									
25 February 2019	1,364p	1,675	30 Sep 2021	30 Sep 2021	–	122,801	–	–	122,801
Nigel Lingwood									
22 December 2016	997.5p	549	30 Sep 2019	30 Sep 2019	55,035	–	55,035	–	–
28 December 2017	1,221p	565	30 Sep 2020	30 Sep 2020	46,294	–	–	–	46,294
7 December 2018	1,209p	749	30 Sep 2021	30 Sep 2021	–	61,917	–	–	61,917

1 The award for Johnny Thomson is set at the level of 250% of base salary, as announced at the time of his appointment to the Board.

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

The PSP awards are granted in the form of nil-cost options (there is a notional exercise price of £1 per award). To the extent that the awards vest, the options are then exercisable until the tenth anniversary of the award date. Details of options exercised during the year and outstanding at 30 September 2019 are set out on page 58.

Services from external advisors (unaudited)

Stephenson Harwood LLP provide legal advice to the Committee on remuneration matters and on the Directors' Remuneration Policy. Ashurst LLP provided legal advice on employment matters. The Committee also received advice and assistance from Aon in connection with the Committee's review of the Company's Remuneration Policy this year. The Committee also engaged MEIS to provide certain data analyses to the Committee. The fees are agreed in advance with the advisor, based on the scope of work.

The fees set out below include advice provided to the Committee and the Board relating to the termination of Richard Ingram as CEO in August 2018. The compensation agreement was approved by both parties on 8 November 2018.

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

Advisor	Appointed by	Services provided to the Committee	Other services provided to the Company	Fees (£)
Aon	Committee	Remuneration advice	None	52,209
MEIS	Committee	Data analysis	None	7,000
Stephenson Harwood LLP	Committee	Legal and remuneration advice	None	27,050
Ashurst	Committee	Legal advice	None	150,284

Shareholder voting at previous Annual General Meeting (unaudited)

The Remuneration Committee's Annual Report ("Report") for the year ended 30 September 2018 was approved by shareholders at the AGM held on 16 January 2019 and the Directors' Remuneration Policy was approved by shareholders at the AGM held on 17 January 2018, with the following votes being cast:

	Policy		Report	
Votes for	91,393,536	97.92%	90,281,418	96.10%
Votes against	1,941,428	2.08%	3,663,518	3.90%
Withheld	12,500	-	390,458	-

Aligning pay with performance (unaudited)

The graph below shows the Total Shareholder Return ("TSR") performance of Diploma PLC for the ten-year period ended 30 September 2019 against the FTSE 250 Index (excluding Investment Trusts) as the Company is a member of this Index.

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



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

Remuneration Committee Report continued

ANNUAL REPORT ON REMUNERATION CONTINUED

Chief Executive Officer remuneration compared with annual growth in TSR (unaudited)

Year	Name	Chief Executive Officer single figure of total remuneration (£000)	Annual bonus against maximum opportunity	Actual share award vesting	Annual growth in TSR
2019	Johnny Thomson ²	1,079	72%	–	+20%
2019	John Nicholas ¹	62	–	–	+20%
2018	John Nicholas ¹	14	–	–	+36%
2018	Richard Ingram ²	235	–	–	+36%
2018	Bruce Thompson ²	3,842	100%	99%	+36%
2017	Bruce Thompson	2,258	100%	89%	+24%
2016	Bruce Thompson	1,634	95%	45%	+36%
2015	Bruce Thompson	1,139	51%	25%	-1%
2014	Bruce Thompson	1,846	65%	61%	+8%
2013	Bruce Thompson	2,401	33%	100%	+42%
2012	Bruce Thompson	1,830	95%	100%	+54%
2011	Bruce Thompson	1,701	100%	100%	+16%
2010	Bruce Thompson	1,287	100%	100%	+71%

1 John Nicholas was not eligible for an annual bonus or share award for service as interim Executive Chairman for the period 28 August 2018 to 25 February 2019.

2 These amounts were prorated for the period served as CEO, with the exception of the annual bonus payable to Johnny Thomson, who joined the Company on 25 February 2019.

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

	Change in base salary	Change in pension	Change in benefits	Change in annual performance bonus
Chief Executive Officer ¹	–	–	–	–
Senior management cadre	4.5%	4.5%	–	-1.0%

1 No change in base salary as Johnny Thomson was appointed as CEO on 25 February 2019.

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

Relative importance of Executive Director remuneration (unaudited)

	2019 £m	2018 £m	Change £m
Total employee remuneration	100.7	92.7	+8.0
Total dividends paid	29.8	26.8	+3.0

Executive Directors' interests
In options over shares

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

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

The nil cost options outstanding at 30 September 2019 and the movements during the year are as follows:

	Year of vesting	Options as at 1 Oct 2018	Exercised in year	Vested during the year	Options unexercised as at 30 Sep 2019	Exercise price	Earliest normal exercise date	Expiry date
Nigel Lingwood	2018	73,063	73,063	–	–	£1	Nov 2018	Dec 2025
	2019	–	–	55,035	55,035	£1	Nov 2019	Dec 2026

1 Nigel Lingwood exercised 73,063 options on 7 December 2018, at a market price of 1,209p per share and the total proceeds before tax were £883,332.

2 On 7 December 2018, the aggregate number of shares received by the participant was reduced by 34,340 shares as part of arrangements under which the Company settled the PAYE liability that arose as a result of the exercise in full by the Executive Director of options held over shares. The market price at that time was 1,209p.

3 The closing price of an ordinary share on 30 September 2019 was 1,663p (2018: 1,416p).

4 All awards have a notional exercise price of £1 per award.

In ordinary shares

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

	As at 30 Sep 2019			As at 30 Sep 2018		
	Ordinary shares	Options vested but unexercised	Interest in shares with performance measures	Ordinary shares	Options vested but unexercised	Interest in shares with performance measures
Johnny Thomson ¹	22,000	–	122,801	–	–	–
Nigel Lingwood	100,000	55,035	108,211	180,000	73,063	101,329

¹ Johnny Thomson's interests are shown following his appointment on 25 February 2019.

As of 18 November 2019, there have been no changes to these interests in ordinary shares of the Company.

At 30 September 2019, the ordinary shares held by Johnny Thomson and Nigel Lingwood represented 55% and 500% of their respective base salaries. As set out on page 47, the Committee has set a minimum shareholding requirement of 250% for the Chief Executive Officer and at least 200% for other Executive Directors.

Chairman and non-Executive Directors' remuneration

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

	Total fees	
	2019 £000	2018 £000
John Nicholas	149	145
Charles Packshaw	62	55
Andy Smith	64	55
Anne Thorburn	64	55

The non-Executive Directors received a basic annual fee of £51,500 during the year and additional fees are paid of £12,000 (2018: £5,000) for chairing a Committee of the Board or £10,000 (2018: 5,000) for acting as Senior Independent Director. No additional fee for chairing a Committee of the Board is payable to the Chairman of the Company. The fees for non-Executive Directors are reviewed every year by the Board, taking into account their responsibilities and required time commitment. Following a review undertaken on 12 November 2019, the Board approved an increase of 3% in the Chairman's fee to £153,400 p.a. and in the basic annual fee paid to non-Executive Directors to £53,000. The additional fee for chairing a Committee of the Board remains at £12,000 and for acting as Senior Independent Director remains at £10,000. All these fee increases will take effect from 1 October 2019. There were no taxable expenses for non-Executive Directors in 2019.

Chairman and non-Executive Directors' interests in ordinary shares

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

	Interest in ordinary shares	
	As at 30 Sep 2019	As at 30 Sep 2018
John Nicholas	7,000	7,000
Charles Packshaw	1,500	1,500
Andy Smith	5,500	5,500
Anne Thorburn	3,000	3,000

As of 18 November 2019, there have been no changes to these interests in ordinary shares of the Company.

Senior executives below the Board (unaudited)

The policies and practices with regard to the remuneration of senior executives below the Executive Directors are generally treated consistently with the Executive Directors. These senior executives all have a significant portion of their reward package linked to performance. Annual bonuses are linked to short term financial targets which use similar performance metrics to the targets for the Executive Directors. Members of the Executive Management Committee ("EMC") participate in the Diploma PLC 2011 PSP described further on page 49. Senior management outside the EMC participate in cash based long term incentive plans which are focused on the operating profit growth of their businesses over rolling three-year periods.

Set out below is a summary of the share-based awards outstanding at 30 September 2019 which have been granted to members of the Executive Management Committee, including share awards which have vested during the year based on performance and share awards which have been granted both last year and during this year. The awards set out below were granted based on a face value limit that varied between 30% and 75% of base salary. No awards will vest unless the performance conditions set out on page 55 are achieved over a three-year measurement period. The Committee anticipates making similar awards to members of the Executive Management Committee in December 2019.

Diploma PLC 2011 Performance Share Plan

	Market price at date of award	Face value of the award at date of grant £000	End of performance period	Maturity date	Shares over which awards held at 1 Oct 2018	Shares over which awards granted during the year	Vested during the period	Lapsed during the period	Shares over which awards held at 30 Sep 2019
22 December 2016	997.5p	390	30 Sep 2019	30 Sep 2019	21,081	–	21,081	–	–
28 December 2017	1,221p	430	30 Sep 2020	30 Sep 2020	18,498	–	–	5,867	12,631
7 December 2018 and 25 February 2019	1,209p/ 1,364p	741	30 Sep 2021	30 Sep 2021	–	60,408	–	18,417	41,991

Directors' Report

This section comprises information which the Directors are required by law and regulation to include within the Annual Report & Accounts. The Directors who held office during the year are set out on pages 34 and 35.

Shareholders

Incorporation and principal activity

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

The principal activity of the Group is the supply of specialised technical products and services. A description and review of the activities of the Group during the financial year including the Company's business model and strategy, principal risks and uncertainties facing the Group and how these are managed and mitigated, together with an indication of future developments is set out in the Strategic Report on pages 1 to 33, which incorporates the requirements of the Companies Act 2006 ("the Act").

Annual General Meeting

The Annual General Meeting ("AGM") will be held at midday on Wednesday, 15 January 2020 in the Pewterers Hall, Oat Lane, London EC2V 7DE. The Notice of the AGM, which is a separate document, will be sent to all shareholders and will be published on the Diploma PLC website.

Substantial shareholdings

At 30 September 2019, the Company had been notified of the following interests amounting to 3% or more of the voting rights in its ordinary share capital:

	Percentage of ordinary share capital
Mawer Investment Management Limited	9.79
Standard Life Aberdeen plc	6.36
Capital Research Global Investors	5.21
Fidelity Management & Research Co.	5.00
Royal London Group	4.95
The Vanguard Group, Inc.	3.42
Mondrian Investment Partners Limited	3.14
Norges Bank Investment Management	3.10

As far as the Directors are aware, there were no changes between 30 September 2019 and 18 November 2019 (the date of this Report) and there were no other interests above 3% of the issued ordinary share capital.

Share capital

The rights attaching to the Company's ordinary shares, as well as the powers of the Company's Directors, are set out in the Company's Articles of Association ("the Articles"), a copy of which is available on the Company's website. The Articles may be amended by special resolution of the Company's shareholders.

Shareholders

Shareholders are entitled to attend and speak at general meetings of the Company and to appoint one or more proxies or, corporate representatives. On a show of hands each holder of ordinary shares shall have one vote, as shall proxies. On a poll, every holder of ordinary shares present in person or by proxy shall have one vote for every share of which they are the holder. Electronic and paper proxy appointments and voting instructions must be received not later than 48 hours before a general meeting.

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

Restrictions on transfer of shares

The Directors may refuse to register a transfer of a certificated share that is not fully paid, provided that the refusal does not prevent dealings in shares in the Company from taking place on an open and

proper basis, or where the Company has lien over that share. The Directors may also refuse to register a transfer of a certificated share, unless the instrument of transfer is: (i) lodged, duly stamped (if necessary), at the registered office of the Company or any other place as the Board may decide accompanied by the certificate for the share(s). Transfers of uncertificated shares must be carried out using CREST and the Directors can refuse to register a transfer of an uncertificated share.

Participants in the Company's Performance Share Plan ("PSP"), who have yet to meet shareholding requirements, have vested PSP shares held in trust until the earlier occurrence of them meeting their shareholder requirement or for a period of two years, during which period these shares cannot be transferred to them. Executive Directors who participate in the Annual Performance Bonus Plan, who have yet to meet shareholding requirements, have 50% of their net annual bonus held in shares until the earlier occurrence of them meeting their shareholding requirement or five years, during which period these shares are held by a nominee.

Share allotment

A general allotment power and a limited power to allot shares in specific circumstances for cash, otherwise than pro rata to existing shareholders, were given to the Directors by resolutions approved at the AGM of the Company held on 16 January 2019. In the year ended 30 September 2019, the Company has not allotted any shares.

Authority to make market purchases of own shares

An authority to make market purchases of up to 10% of the issued share capital shares was given to the Directors by a special resolution at the AGM of the Company held on 16 January 2019. In the year to 30 September 2019, the Company has not acquired any of its own shares.

Disclosures required under Listing Rule 9.8.4R

There is no information to be disclosed by the Company in respect of Listing Rule 9.8.4R, except for ordinary shares held within the Diploma PLC Employee Benefit Trust. The voting rights are exercisable by the Trustees in accordance with their fiduciary duties. The Trustees of the Diploma PLC Employee Benefit Trust also waive dividends on all shares.

Contracts of significance and change of control

There are a number of agreements that take effect, alter or terminate upon a change of control of the Company, principally bank facility agreements, the Company's Long Term Incentive Plan and the Annual Performance Bonus Plan.

Non-financial information

The Company has chosen, in accordance with s414C(11) of the Companies Act 2006, to include certain matters in its Strategic Report on pages 1 and 33 that would otherwise be required to be disclosed in this Directors' Report.

Non-financial information statement

Other information that is relevant to the Directors' Report and which is incorporated by reference into this Report, can be viewed in the section on Corporate Responsibility on pages 32 and 33 and includes:

Our employees	Environmental matters
Health & Safety	Greenhouse gas emissions
Human rights	Business ethics, corruption and bribery
Modern slavery	Community

Other related information can also be found as follows:

Business model – pages 6 to 9.
Principal risks and how they are managed or mitigated – pages 28 to 31.
Non-financial key performance indicators – pages 11 and 32.

Financial Results and dividends

The profit for the financial year attributable to shareholders was £61.9m (2018: £53.8m). The Directors recommend a final dividend of 20.5p per ordinary share (2018: 17.8p), to be paid, if approved, on 22 January 2020. This, together with the interim dividend of 8.5p (2018: 7.7p) per ordinary share paid on 12 June 2019 amounts to 29.0p for the year (2018: 25.5p).

The results are shown more fully in the consolidated financial statements on pages 62 to 88 and summarised in the Finance Review on pages 24 to 27.

Auditor

Each of the persons who is a Director at the date of approval of this Annual Report & Accounts confirms that so far as the Director is aware, there is no relevant audit information of which the Company's Auditor is unaware; and the Director has taken all the steps that he/she ought to have taken as a Director in order to make himself/herself aware of any relevant audit information and to establish that the Company's Auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

PricewaterhouseCoopers LLP ("PwC") has expressed its willingness to continue in office as independent auditor and a resolution to reappoint PwC will be proposed at the AGM to be held on 15 January 2020.

Directors' assessment of going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 1 to 33. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Finance Review on pages 24 to 27. In addition, pages 75 to 77 of the Annual Report & Accounts include the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

The Group has considerable financial resources, together with a broad spread of customers and suppliers across different geographic areas and sectors, often secured with longer term agreements. As a consequence, the Directors believe that the Group is well placed to manage its business risks successfully as described further on pages 28 to 31.

The Group also has a committed multi-currency revolving bank facility of £30.0m with an accordion option to increase the committed facility by a further £30.0m up to a maximum of £60.0m. This facility expires on 1 June 2022. On 8 July 2019, the Company entered into a term loan facility of an aggregate principal amount of £40.0m to assist in the funding of the acquisition of VSP Technologies. At 30 September 2019, the Group had net debt of £15.1m comprising cash funds of £27.0m and £42.1m borrowings.

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

Statement of Directors' responsibilities for preparing the financial statements

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

Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. Under that law the Directors are required to prepare Group financial statements in accordance with IFRS as adopted by the European Union ("EU") and Article 4 of the IAS Regulations and have elected to prepare the Parent Company financial statements in accordance with United Kingdom Generally Accepted Accounting Standards (UK Accounting Standards) including FRS101 (*Reduced Disclosures Framework*).

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

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

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

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

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

Directors' Responsibility Statement

The Directors confirm that to the best of their knowledge:

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

This responsibility statement was approved by the Board of Directors on 18 November 2019 and is signed on its behalf by:

JD Thomson
Chief Executive Officer

NP Lingwood
Group Finance Director

Registered office:
12 Charterhouse Square
London
EC1M 6AX

Registered Number: 3899848

Consolidated Income Statement

For the year ended 30 September 2019

	Note	2019 £m	2018 £m
Revenue	3,4	544.7	485.1
Cost of sales		(347.7)	(312.2)
Gross profit		197.0	172.9
Distribution costs		(12.7)	(10.8)
Administration costs		(100.2)	(88.9)
Operating profit	3	84.1	73.2
Financial expense, net	6	(0.6)	(0.5)
Profit before tax		83.5	72.7
Tax expense	7	(21.1)	(18.3)
Profit for the year		62.4	54.4
Attributable to:			
Shareholders of the Company		61.9	53.8
Minority interests	21	0.5	0.6
		62.4	54.4
Earnings per share			
Basic and diluted earnings	9	54.7p	47.5p

Alternative Performance Measures (Note 2)

	Note	2019 £m	2018 £m
Operating profit		84.1	73.2
Add: Acquisition related charges	11	13.1	9.6
Add: CEO transition costs		-	2.1
Adjusted operating profit	3,4	97.2	84.9
Deduct: Interest expense	6	(0.7)	(0.1)
Adjusted profit before tax		96.5	84.8
Adjusted earnings per share	9	64.3p	56.4p

The notes on pages 66 to 88 form part of these consolidated financial statements.

Consolidated Statement of Comprehensive Income

For the year ended 30 September 2019

	Note	2019 £m	2018 £m
Profit for the year		62.4	54.4
Items that will not be reclassified to the Consolidated Income Statement			
Actuarial losses in the defined benefit pension schemes	25	(7.2)	(1.0)
Deferred tax on items that will not be reclassified	7,14	1.3	0.2
		(5.9)	(0.8)
Items that may be reclassified to Consolidated Income Statement			
Exchange rate gains on foreign currency net investments		6.2	0.1
Gains on fair value of cash flow hedges	19	0.4	0.7
Net changes to fair value of cash flow hedges transferred to the Consolidated Income Statement	19	(0.7)	0.9
Deferred tax on items that may be reclassified	7,14	-	(0.4)
		5.9	1.3
Total Comprehensive Income for the year		62.4	54.9
Attributable to:			
Shareholders of the Company		61.9	54.2
Minority interests		0.5	0.7
		62.4	54.9

Consolidated Statement of Changes in Equity

For the year ended 30 September 2019

	Note	Share capital £m	Translation reserve £m	Hedging reserve £m	Retained earnings £m	Shareholders' equity £m	Minority interests £m	Total equity £m
At 1 October 2017		5.7	29.7	(0.7)	227.3	262.0	4.8	266.8
Total Comprehensive Income		-	0.1	1.2	52.9	54.2	0.7	54.9
Share-based payments	5	-	-	-	1.0	1.0	-	1.0
Minority interests acquired	21	-	-	-	2.5	2.5	(2.5)	-
Minority interest contribution	21	-	-	-	-	-	0.3	0.3
Tax on items recognised directly in equity	7	-	-	-	0.5	0.5	-	0.5
Notional purchase of own shares		-	-	-	(2.2)	(2.2)	-	(2.2)
Dividends	8,21	-	-	-	(26.8)	(26.8)	(0.2)	(27.0)
At 30 September 2018		5.7	29.8	0.5	255.2	291.2	3.1	294.3
Total Comprehensive Income		-	6.2	(0.3)	56.0	61.9	0.5	62.4
Share-based payments	5	-	-	-	0.8	0.8	-	0.8
Minority interests acquired		-	-	-	-	-	-	-
Minority interest contribution		-	-	-	-	-	-	-
Tax on items recognised directly in equity	7	-	-	-	0.1	0.1	-	0.1
Notional purchase of own shares		-	-	-	(2.9)	(2.9)	-	(2.9)
Dividends	8,21	-	-	-	(29.8)	(29.8)	(0.3)	(30.1)
At 30 September 2019		5.7	36.0	0.2	279.4	321.3	3.3	324.6

The notes on pages 66 to 88 form part of these consolidated financial statements.

Consolidated Statement of Financial Position

As at 30 September 2019

	Note	2019 £m	2018 £m
Non-current assets			
Goodwill	10	155.0	128.5
Acquisition intangible assets	11	96.1	53.6
Other intangible assets	11	2.7	1.8
Investment	12	–	0.7
Property, plant and equipment	13	26.7	23.0
Deferred tax assets	14	0.5	0.3
		281.0	207.9
Current assets			
Inventories	15	102.6	82.9
Trade and other receivables	16	91.1	77.6
Cash and cash equivalents	18	27.0	36.0
		220.7	196.5
Current liabilities			
Trade and other payables	17	(90.2)	(80.5)
Current tax liabilities	7	(6.9)	(4.8)
Other liabilities	20	(10.8)	(5.6)
		(107.9)	(90.9)
Net current assets		112.8	105.6
Total assets less current liabilities		393.8	313.5
Non-current liabilities			
Retirement benefit obligations	25	(17.8)	(10.5)
Borrowings	24	(42.1)	–
Other liabilities	20	(0.5)	–
Deferred tax liabilities	14	(8.8)	(8.7)
Net assets		324.6	294.3
Equity			
Share capital		5.7	5.7
Translation reserve		36.0	29.8
Hedging reserve		0.2	0.5
Retained earnings		279.4	255.2
Total shareholders' equity		321.3	291.2
Minority interests	21	3.3	3.1
Total equity		324.6	294.3

The consolidated financial statements were approved by the Board of Directors on 18 November 2019 and signed on its behalf by:

JD Thomson
Chief Executive Officer

NP Lingwood
Group Finance Director

The notes on pages 66 to 88 form part of these consolidated financial statements.

Consolidated Cash Flow Statement

For the year ended 30 September 2019

	Note	2019 £m	2018 £m
Operating profit		84.1	73.2
Acquisition related charges	23	13.1	9.6
CEO transition costs, (paid)/unpaid	23	(1.3)	1.3
Non-cash items	23	5.8	5.3
Increase in working capital	23	(9.4)	(5.1)
Cash flow from operating activities	23	92.3	84.3
Interest paid, net		(0.1)	-
Tax paid		(21.9)	(19.0)
Net cash from operating activities		70.3	65.3
Cash flow from investing activities			
Acquisition of businesses (net of expenses and cash acquired)	22	(77.2)	(18.1)
Deferred consideration paid	20	(1.1)	(0.3)
Proceeds from sale of business (net of expenses)		-	4.0
Purchase of property, plant and equipment	13	(9.7)	(5.3)
Purchase of other intangible assets	11	(1.2)	(1.3)
Proceeds from sale of property, plant and equipment		-	-
Net cash used in investing activities		(89.2)	(21.0)
Cash flow from financing activities			
Acquisition of minority interests	20	-	(2.0)
Dividends paid to shareholders	8	(29.8)	(26.8)
Dividends paid to minority interests	21	(0.3)	(0.2)
Purchase of own shares by Employee Benefit Trust		(1.2)	(1.2)
Notional purchase of own shares on exercise of share options		(1.7)	(1.0)
Proceeds from borrowings	24	41.1	-
Net cash from/(used in) financing activities		8.1	(31.2)
Net (decrease)/increase in cash and cash equivalents		(10.8)	13.1
Cash and cash equivalents at beginning of year		36.0	22.3
Effect of exchange rates on cash and cash equivalents		1.8	0.6
Cash and cash equivalents at end of year	18	27.0	36.0

Alternative Performance Measures (Note 2)

	Note	2019 £m	2018 £m
Net (decrease)/increase in cash and cash equivalents		(10.8)	13.1
Add: Dividends paid to shareholders	8	29.8	26.8
Dividends paid to minority interests	21	0.3	0.2
Acquisition of businesses (net of expenses and cash acquired)	22	77.2	18.1
Acquisition of minority interests	20	-	2.0
Deferred consideration paid	20	1.1	0.3
Proceeds from borrowings	24	(41.1)	-
Free cash flow		56.5	60.5
Cash and cash equivalents		27.0	36.0
Borrowings		(42.1)	-
(Net debt)/cash funds	24	(15.1)	36.0

Notes to the Consolidated Financial Statements

For the year ended 30 September 2019

1. General information

Diploma PLC is a public limited company registered and domiciled in England and Wales and listed on the London Stock Exchange. The address of the registered office is 12 Charterhouse Square, London EC1M 6AX. The consolidated financial statements comprise the Company and its subsidiaries (together referred to as "the Group") and were authorised by the Directors for publication on 18 November 2019. These statements are presented in UK sterling, with all values rounded to the nearest 100,000, except where otherwise indicated.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRSs"), as adopted by the European Union ("EU") and in accordance with the Companies Act 2006, as applicable to companies reporting under IFRS. The financial statements of the Parent Company, Diploma PLC, have been prepared in accordance with *FRS101 (Reduced Disclosure Framework)* and are set out in a separate section of the Annual Report & Accounts on pages 89 and 90.

2. Alternative performance measures

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

2.1 Adjusted operating profit

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

2.2 Adjusted profit before tax

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

2.3 Adjusted earnings per share

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

2.4 Free cash flow

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

2.5 Trading capital employed and ROATCE

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

3. Business Sector analysis

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

For management reporting purposes, the Group is organised into three main reportable business Sectors: Life Sciences, Seals and Controls. These Sectors are the Group's operating segments as defined by IFRS8 and form the basis of the primary reporting format disclosures below. The CODM reviews discrete financial information at these operating segments level. The principal activities of each of these Sectors is described in the Strategic Report on pages 1 to 33. Sector revenue represents revenue from external customers; there is no inter-Sector revenue. Sector results, assets and liabilities include items directly attributable to a Sector, as well as those that can be allocated on a reasonable basis.

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

3. Business Sector analysis continued

	Life Sciences		Seals		Controls		Group	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Revenue – existing	145.7	134.7	211.3	208.0	168.3	142.4	525.3	485.1
Revenue – acquisitions	0.1	–	9.3	–	10.0	–	19.4	–
Revenue	145.8	134.7	220.6	208.0	178.3	142.4	544.7	485.1
Adjusted operating profit – existing	27.4	23.9	36.4	36.0	30.1	25.0	93.9	84.9
Adjusted operating profit – acquisitions	0.1	–	1.7	–	1.5	–	3.3	–
Adjusted operating profit	27.5	23.9	38.1	36.0	31.6	25.0	97.2	84.9
Acquisition related charges	(2.3)	(2.4)	(7.0)	(5.0)	(3.8)	(2.2)	(13.1)	(9.6)
CEO transition costs	–	–	–	–	–	–	–	(2.1)
Operating profit	25.2	21.5	31.1	31.0	27.8	22.8	84.1	73.2

	Life Sciences		Seals		Controls		Group	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Operating assets	45.6	43.5	109.6	80.1	65.6	59.3	220.8	182.9
Investment	–	–	–	0.7	–	–	–	0.7
Goodwill	64.0	59.0	59.1	40.3	31.9	29.2	155.0	128.5
Acquisition intangible assets	15.6	12.9	61.7	21.8	18.8	18.9	96.1	53.6
	125.2	115.4	230.4	142.9	116.3	107.4	471.9	365.7
Unallocated assets:								
– Deferred tax assets							0.5	0.3
– Cash and cash equivalents							27.0	36.0
– Corporate assets							1.9	2.4
Total assets	125.2	115.4	230.4	142.9	116.3	107.4	501.3	404.4
Operating liabilities	(25.3)	(21.6)	(37.1)	(32.2)	(27.6)	(25.5)	(90.0)	(79.3)
Unallocated liabilities:								
– Deferred tax liabilities							(8.8)	(8.7)
– Retirement benefit obligations							(17.8)	(10.5)
– Acquisition liabilities							(11.3)	(5.6)
– Corporate liabilities							(6.7)	(6.0)
– Borrowings							(42.1)	–
Total liabilities	(25.3)	(21.6)	(37.1)	(32.2)	(27.6)	(25.5)	(176.7)	(110.1)
Net assets	99.9	93.8	193.3	110.7	88.7	81.9	324.6	294.3

Alternative Performance Measures (Note 2)

	Life Sciences		Seals		Controls		Group	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Net assets	99.9	93.8	193.3	110.7	88.7	81.9	324.6	294.3
Add/(deduct):								
– Deferred tax, net							8.3	8.4
– Retirement benefit obligations							17.8	10.5
– Acquisition liabilities							11.3	5.6
– Net debt/(cash and cash equivalents)							15.1	(36.0)
Reported trading capital employed							377.1	282.8
– Historic goodwill and acquisition related charges, net of deferred tax	32.0	31.4	39.2	33.0	13.1	10.2	84.3	74.6
Adjusted trading capital employed	131.9	125.2	232.5	143.7	101.8	92.1	461.4	357.4
Pro forma adjusted operating profit ¹	29.0	23.9	44.9	36.3	31.6	27.4	105.5	87.6
ROATCE	22.0%	19.1%	19.3%	25.3%	31.0%	29.8%	22.9%	24.5%

¹ After annualisation of adjusted operating profit of acquisitions and disposals (note 22).

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

3. Business Sector analysis continued

Other Sector information

	Life Sciences		Seals		Controls		Group	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Capital expenditure	3.3	3.5	5.1	2.0	2.5	1.1	10.9	6.6
Depreciation and amortisation	2.7	2.4	2.0	1.8	0.7	0.6	5.4	4.8
Revenue recognition								
– immediately on sale	131.8	122.5	219.5	206.9	178.3	142.4	529.6	471.8
– over a period of time	14.0	12.2	1.1	1.1	–	–	15.1	13.3
	145.8	134.7	220.6	208.0	178.3	142.4	544.7	485.1

Accrued income (“contract assets”) at 30 September 2019 of £1.5m (2018: £1.6m) and deferred revenue (“contract liabilities”) of £2.6m at 30 September 2019 (2018: £2.4m) is included in trade and other receivables (note 16) and trade and other payables (note 17), respectively.

4. Geographic segment analysis by origin

	Revenue		Adjusted operating profit		Non-current assets ¹		Trading capital employed		Capital expenditure	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
United Kingdom	154.8	130.2	27.8	23.5	59.0	54.1	84.5	79.2	2.0	0.6
Rest of Europe	128.1	115.2	18.6	17.6	58.9	57.0	80.4	76.9	1.7	1.5
North America	220.5	202.3	45.0	39.5	129.8	70.5	176.2	97.1	6.5	4.0
Rest of world	41.3	37.4	5.8	4.3	32.8	25.3	36.0	29.6	0.7	0.5
	544.7	485.1	97.2	84.9	280.5	206.9	377.1	282.8	10.9	6.6

¹ Non-current assets exclude investments and deferred tax assets.

5. Group employee costs

Average number of employees

	2019	2018
Life Sciences	434	420
Seals	861	857
Controls	584	471
Corporate	17	17
Number of employees – average	1,896	1,765
Number of employees – year end	2,064	1,803

Group employee costs, including key management

	2019 £m	2018 £m
Wages and salaries	87.5	81.2
Social security costs	8.6	7.4
Pension costs	3.8	3.1
Share-based payments	0.8	1.0
	100.7	92.7

Key management short term remuneration, including Directors

	2019 £m	2018 £m
Salaries and short term employee benefits	3.8	3.6
Pension costs	0.2	0.3
Share-based payments	0.8	1.0
	4.8	4.9

The Group considers key management personnel as defined in IAS24 (*Related Party Disclosures*) to be the Directors of the Company and the members of the Executive Management Committee (“EMC”).

The Executive Directors’ remuneration and their interests in shares of the Company are given on pages 54 to 59 in the Remuneration Committee Report. The EMC’s interests in the Group’s LTIP is set out on page 59. The charge for share-based payments of £0.8m (2018: £1.0m) relates to the Group’s LTIP, described in the Remuneration Committee Report.

Directors’ short term remuneration

	2019 £m	2018 £m
Non-executive Directors	0.3	0.3
Executive Directors	1.8	2.0
	2.1	2.3

6. Financial expense, net

	2019 £m	2018 £m
Interest (expense)/income and similar charges		
– bank facility and commitment fees	(0.2)	(0.1)
– interest income on bank deposits	0.1	0.1
– interest expense on bank borrowings	(0.4)	–
– notional interest expense on the defined benefit pension scheme (note 25b)	(0.2)	(0.1)
Net interest expense and similar charges	(0.7)	(0.1)
– fair value remeasurement of financial liabilities and unwind of discount (note 20)	0.1	(0.4)
Financial expense, net	(0.6)	(0.5)

The fair value remeasurement of £0.1m credit (2018: £0.4m debit) comprises £0.1m debit (2018: £Nil) that relates to the unwinding of the discount on the liability for deferred consideration in respect of the acquisition of VSP Technologies and of a movement in the fair value of the put options of £0.2m credit (2018: £0.2m debit). There is no impact (2018: £0.2m debit) for future purchases of minority interests as the discount is now fully unwound.

7. Tax expense

	2019 £m	2018 £m
Current tax		
The tax charge is based on the profit for the year and comprises:		
UK corporation tax	4.9	3.9
Overseas tax	17.8	16.1
	22.7	20.0
Adjustments in respect of prior year:		
UK corporation tax	–	–
Overseas tax	0.5	(0.1)
Total current tax	23.2	19.9
Deferred tax		
The net deferred tax credit based on the origination and reversal of timing differences comprises:		
United Kingdom	(0.9)	(0.4)
Overseas	(1.2)	(1.2)
Total deferred tax	(2.1)	(1.6)
Total tax on profit for the year	21.1	18.3

In addition to the above credit for deferred tax included in the Consolidated Income Statement, a net deferred tax balance relating to the retirement benefit scheme and cash flow hedges of £1.3m was credited (2018: £0.2m charge) directly to the Consolidated Statement of Comprehensive Income. A further £0.1m of current tax (2018: £0.5m) was credited to the Consolidated Statement of Changes in Equity which relates to share-based payments made during the year.

Factors affecting the tax charge for the year

The difference between the total tax charge calculated by applying the effective rate of UK corporation tax of 19.0% to the profit before tax of £83.5m and the amount set out above is as follows:

	2019 £m	2018 £m
Profit before tax	83.5	72.7
Tax on profit at UK effective corporation tax rate of 19.0% (2018: 19.0%)	15.9	13.8
Effects of:		
– higher tax rates on overseas earnings	3.8	4.0
– adjustments to current tax charge in respect of previous years	0.5	(0.1)
– other permanent differences	0.9	0.6
Total tax on profit for the year	21.1	18.3

The Group earns its profits in the UK and overseas. The Group prepares its consolidated financial statements for the year to 30 September and the effective tax rate for UK corporation tax in respect of the year ended 30 September 2019 was 19.0% (2018: 19.0%) and this rate has been used for tax on profit in the above reconciliation.

The Group's net overseas tax rate is higher than that in the UK, primarily because profits earned in the US, Canada and Australia are taxed at higher rates than the UK. The UK deferred tax assets and liabilities at 30 September 2019 have been calculated based on the future UK corporation tax rate of 17.0% (2018: 17.0%), as substantively enacted at 30 September 2019.

At 30 September 2019, the Group had outstanding tax liabilities of £6.9m (2018: £4.8m) of which £3.0m (2018: £2.1m) related to UK tax liabilities and £3.9m (2018: £2.7m) related to overseas tax liabilities. These amounts are expected to be paid within the next financial year.

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

8. Dividends

	2019 pence per share	2018 pence per share	2019 £m	2018 £m
Interim dividend, paid in June	8.5	7.7	9.6	8.7
Final dividend of the prior year, paid in January	17.8	16.0	20.2	18.1
	26.3	23.7	29.8	26.8

The Directors have proposed a final dividend in respect of the current year of 20.5p per share (2018: 17.8p), which will be paid on 22 January 2020, subject to approval of shareholders at the Annual General Meeting on 15 January 2020. The total dividend for the current year, subject to approval of the final dividend, will be 29.0p per share (2018: 25.5p).

The Diploma PLC Employee Benefit Trust holds 51,867 (2018: 100,368) shares, which are ineligible for dividends.

9. Earnings per share

Basic and diluted earnings per share

Basic and diluted earnings per ordinary 5p share are calculated on the basis of the weighted average number of ordinary shares in issue during the year of 113,179,582 (2018: 113,140,435) and the profit for the year attributable to shareholders of £61.9m (2018: £53.8m). Further description of the Company's share capital is set out in note (e) to the Parent Company Financial Statements on page 90.

Adjusted earnings per share

Adjusted EPS, which is defined in note 2, is calculated as follows:

	2019 pence per share	2018 pence per share	2019 £m	2018 £m
Profit before tax			83.5	72.7
Tax expense			(21.1)	(18.3)
Minority interests			(0.5)	(0.6)
Earnings for the year attributable to shareholders of the Company	54.7	47.5	61.9	53.8
Acquisition related charges	11.6	8.4	13.1	9.6
Fair value remeasurement of financial liabilities and unwind of discount	(0.1)	0.4	(0.1)	0.4
CEO transition costs	–	1.8	–	2.1
Tax effects on above adjustments	(1.9)	(1.7)	(2.1)	(2.0)
Adjusted earnings	64.3	56.4	72.8	63.9

10. Goodwill

	Life Sciences £m	Seals £m	Controls £m	Total £m
At 1 October 2017	59.5	39.9	23.4	122.8
Acquisitions	–	–	5.7	5.7
Exchange adjustments	(0.5)	0.4	0.1	–
At 30 September 2018	59.0	40.3	29.2	128.5
Acquisitions (note 22)	3.9	17.5	2.7	24.1
Exchange adjustments	1.1	1.3	–	2.4
At 30 September 2019	64.0	59.1	31.9	155.0

The Group tests goodwill for impairment at least once a year. For the purposes of impairment testing, goodwill is allocated to each of the Group's three cash-generating units, which are the three operating Sectors: Life Sciences; Seals; and Controls. This represents the lowest level within the Group at which goodwill is monitored by management and reflects the Group's strategy of acquiring businesses to drive synergies across a Sector, rather than within an individual business. The impairment test requires a "value in use" valuation to be prepared for each Sector using discounted cash flow forecasts. The cash flow forecasts are based on a combination of annual budgets prepared by each business and the Group's strategic plan. Beyond five years, cash flow projections utilise a perpetuity growth rate of 2%.

The key assumptions used to prepare the cash flow forecasts relate to gross margins, revenue growth rates and the discount rate. The gross margins are assumed to remain sustainable, which is supported by historical experience; revenue growth rates generally approximate to the average rates for the markets in which the business operates, unless there are particular factors relevant to a business, such as start-ups. The annual revenue growth rates used in the cash flow forecasts for the next five years represent the budgeted rates for 2020 and thereafter, average growth rates for each Sector; these annual growth rates then reduce to 2% over the longer term.

The cash flow forecasts are discounted to determine a current valuation using a single market derived pre-tax discount rate of ca. 11% (2018: 11%). This single rate is based on the characteristics of lower risk, non-technically driven, distribution businesses operating generally in well developed markets and geographies and with robust capital structures. As these features are consistent between each of the Group's Sectors, the Board considers that it is appropriate to use a single discount rate applied to each Sector's cash flow forecasts.

Based on the criteria set out above, no impairment in the value of goodwill in any of the Sectors was identified.

The Directors have also carried out sensitivity analysis on the key assumptions noted above to determine whether a "reasonably possible adverse change" in any of these assumptions would result in an impairment of goodwill. The analysis indicates that a "reasonably possible adverse change" would not give rise to an impairment charge to goodwill in any of the three Sectors.

11. Acquisition and other intangible assets

	Customer relationships £m	Supplier relationships £m	Trade names and databases £m	Total acquisition intangible assets £m	Other intangible assets £m
Cost					
At 1 October 2017	80.2	29.6	2.8	112.6	5.6
Additions	–	–	–	–	1.3
Acquisitions (note 22)	9.1	–	–	9.1	–
Disposals	–	–	–	–	(0.2)
Exchange adjustments	0.3	(0.1)	–	0.2	0.1
At 30 September 2018	89.6	29.5	2.8	121.9	6.8
Additions	–	–	–	–	1.2
Acquisitions (note 22)	53.2	–	–	53.2	–
Disposals	–	–	–	–	–
Exchange adjustments	2.1	0.2	0.2	2.5	0.3
At 30 September 2019	144.9	29.7	3.0	177.6	8.3
Amortisation					
At 1 October 2017	40.7	15.3	2.6	58.6	4.9
Charge for the year	7.1	2.0	0.2	9.3	0.3
Disposals	–	–	–	–	(0.2)
Exchange adjustments	0.4	–	–	0.4	–
At 30 September 2018	48.2	17.3	2.8	68.3	5.0
Charge for the year	9.8	1.8	–	11.6	0.5
Disposals	–	–	–	–	–
Exchange adjustments	1.1	0.3	0.2	1.6	0.1
At 30 September 2019	59.1	19.4	3.0	81.5	5.6
Net book value					
At 30 September 2019	85.8	10.3	–	96.1	2.7
At 30 September 2018	41.4	12.2	–	53.6	1.8

Acquisition related charges are £13.1m (2018: £9.6m) and comprise £11.6m (2018: £9.3m) of amortisation of acquisition intangible assets, £1.5m of acquisition expenses (2018: £0.5m) and £Nil relating to adjustments to deferred consideration (2018: £0.2m credit).

Acquisition intangible assets relate to items acquired through business combinations which are amortised over their useful economic life.

	Economic life
Customer relationships	5–15 years
Supplier relationships	8–10 years
Databases and trade names	5–10 years

Other intangible assets comprise computer software that is separately identifiable from IT equipment and includes software licences.

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

12. Investment

	2019 £m	2018 £m
Investment	–	0.7

In October 2019, the Group concluded its negotiations to dispose of its 10% interest in the share capital of Kunshan J Royal Precision Products Inc. ("JRPP"), a supplier to J Royal, for US\$1.0m. Accordingly, this investment is now classified as an asset held for sale in note 16. The Group had no involvement in the day-to-day operations or management of JRPP.

13. Property, plant and equipment

	Freehold properties £m	Leasehold properties £m	Plant and equipment £m	Hospital field equipment £m	Total £m
Cost					
At 1 October 2017	14.5	3.8	21.1	11.5	50.9
Additions	1.0	0.8	1.2	2.3	5.3
Acquisitions of businesses	–	–	–	–	–
Disposals	–	(0.3)	(2.3)	(0.7)	(3.3)
Exchange adjustments	0.4	(0.2)	0.4	(0.2)	0.4
At 30 September 2018	15.9	4.1	20.4	12.9	53.3
Additions	2.0	0.8	4.2	2.7	9.7
Acquisitions of businesses (note 22)	–	–	0.8	–	0.8
Disposals	–	(0.1)	(0.4)	(0.9)	(1.4)
Reclassification to held for sale	(3.4)	–	–	–	(3.4)
Exchange adjustments	0.5	0.1	0.7	0.6	1.9
At 30 September 2019	15.0	4.9	25.7	15.3	60.9
Depreciation					
At 1 October 2017	4.4	2.0	15.0	6.9	28.3
Charge for the year	0.5	0.4	1.8	1.8	4.5
Disposals	–	(0.2)	(2.2)	(0.4)	(2.8)
Exchange adjustments	0.3	(0.2)	0.3	(0.1)	0.3
At 30 September 2018	5.2	2.0	14.9	8.2	30.3
Charge for the year	0.6	0.5	1.8	2.0	4.9
Disposals	–	–	(0.4)	(0.5)	(0.9)
Reclassification to held for sale	(1.0)	–	–	–	(1.0)
Exchange adjustments	0.2	–	0.4	0.3	0.9
At 30 September 2019	5.0	2.5	16.7	10.0	34.2
Net book value					
At 30 September 2019	10.0	2.4	9.0	5.3	26.7
At 30 September 2018	10.7	2.1	5.5	4.7	23.0

Land included within freehold properties above which is not depreciated is £2.7m (2018: £3.4m). Capital commitments contracted, but not provided, were £3.9m (2018: £0.7m) principally relating to the development of a second warehouse for the Seals Aftermarket business in the US.

Freehold properties include ca. 150 acres of land at Stamford (the "Stamford Land") that comprises mostly farm land and former quarry land.

The Group has entered into a Promotion and Option Agreement with Larkfleet Limited ("Larkfleet") in respect of the Stamford Land.

Under the terms of the Agreement, Larkfleet promotes the site through the planning system. Once satisfactory planning permission is granted, Larkfleet has an option to purchase up to 60% of the residential development land. The remaining land will be sold by the Group in the open market at a time of its choosing.

The initial planning promotion period is six years, but this can be extended by Larkfleet to ten years if it pays an extension fee. Once planning permission has been granted the Agreement extends for up to ten years to allow for marketing and disposal of all of the land benefiting from planning permission to be completed.

The Stamford Land falls within the Stamford North Urban Extension ("SNUE") proposal which sits within the local authority areas of South Kesteven District Council ("SKDC") in Lincolnshire and Rutland County Council ("RCC"). The SNUE is currently under review by the Planning Inspector for the SKDC Local Plan Adoption and is a major allocation within the RCC Draft Local Plan. At 30 September 2019, neither the SKDC or RCC Local Plans are adopted and Larkfleet has not yet submitted a planning application.

In the Directors' opinion the current fair value of its land at 30 September 2019 is £1.0m (2018: £1.0m) with a book value of £Nil.

14. Deferred tax

The movement on deferred tax is as follows:

	2019 £m	2018 £m
At 1 October	(8.4)	(8.2)
Credit for the year (note 7)	2.1	1.6
Acquisitions (note 22)	(3.3)	(1.6)
Accounted for in Other Comprehensive Income	1.3	(0.2)
Exchange adjustments	-	-
At 30 September	(8.3)	(8.4)

Deferred tax assets and liabilities are only offset where there is a legally enforceable right of offset and there is an intention to settle the balances on a net basis.

	Assets		Liabilities		Net	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Property, plant and equipment	0.6	0.6	(1.8)	(1.4)	(1.2)	(0.8)
Goodwill and intangible assets	-	-	(13.4)	(11.7)	(13.4)	(11.7)
Retirement benefit obligations	3.2	2.0	-	-	3.2	2.0
Inventories	1.7	1.5	(0.1)	(0.1)	1.6	1.4
Share-based payments	0.2	0.2	-	-	0.2	0.2
Trading losses	0.1	0.1	-	-	0.1	0.1
Other temporary differences	1.5	0.9	(0.3)	(0.5)	1.2	0.4
	7.3	5.3	(15.6)	(13.7)	(8.3)	(8.4)
Deferred tax offset	(6.8)	(5.0)	6.8	5.0	-	-
	0.5	0.3	(8.8)	(8.7)	(8.3)	(8.4)

No deferred tax has been provided on unremitted earnings of overseas Group companies as the Group controls the dividend policies of its subsidiaries. Unremitted earnings may be liable to overseas withholding tax (after allowing for double taxation relief) if they were to be distributed as dividends. The aggregate amount for which deferred tax has not been recognised in respect of unremitted earnings from overseas businesses of £147.3m was £7.6m (2018: £6.3m).

15. Inventories

	2019 £m	2018 £m
Finished goods	102.6	82.9

Inventories are stated net of impairment provisions of £9.3m (2018: £8.7m). During the year £2.1m (2018: £1.5m) was recognised as a charge against cost of sales, comprising the write-down of inventories to net realisable value.

16. Trade and other receivables

	2019 £m	2018 £m
Trade receivables	82.0	71.5
Less: loss allowance	(1.2)	(0.7)
	80.8	70.8
Other receivables	3.7	3.5
Prepayments and accrued income	3.5	3.3
Assets held for sale	3.1	-
	91.1	77.6

Assets held for sale include one operating facility whereby the freehold property will be sold to a third party and leased back to the business. The Group's investment held in JRPP is also included as an asset held for sale, following conclusion of negotiations in October 2019.

The maximum exposure to credit risk for trade receivables at 30 September, by currency, was:

	2019 £m	2018 £m
UK sterling	25.3	23.8
US dollars	22.2	16.0
Canadian dollars	11.0	10.2
Euro	13.8	12.3
Other	9.7	9.2
	82.0	71.5

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

16. Trade and other receivables continued

Trade receivables, before loss allowance, are analysed as follows:

	2019 £m	2018 £m
Not past due	69.2	59.2
Past due	11.6	11.6
Past due, but impaired	1.2	0.7
	82.0	71.5

The ageing of trade receivables classified as past due, but not impaired, is as follows:

	2019 £m	2018 £m
Up to one month past due	10.0	9.8
Between one and two months past due	1.4	1.4
Between two and four months past due	–	0.4
Over four months past due	0.2	–
	11.6	11.6

The movement in the loss allowance for impairment of trade receivables is as follows:

	2019 £m	2018 £m
At 1 October	0.7	0.8
Charged against profit, net	0.2	(0.1)
Set up on acquisition	0.4	–
Utilised by write-off	(0.1)	–
At 30 September	1.2	0.7

Concentrations of credit risk with respect to trade receivables are very limited reflecting the Group's customer base being large and diverse. The Group has a history of very low levels of losses in respect of trade receivables. Management are satisfied that the loss allowance takes into account the historical loss experience and forward looking expected credit losses in line with IFRS9 (*Financial Instruments*).

17. Trade and other payables

	2019 £m	2018 £m
Trade payables	54.0	48.3
Other payables	5.4	3.6
Other taxes and social security	5.6	4.9
Accruals and deferred income	25.2	23.7
	90.2	80.5

The maximum exposure to foreign currency risk for trade payables at 30 September, by currency, was:

	2019 £m	2018 £m
UK sterling	12.1	11.2
US dollars	25.1	20.2
Canadian dollars	1.2	0.9
Euro	12.8	13.2
Other	2.8	2.8
	54.0	48.3

18. Cash and cash equivalents

	UK £m	US\$ £m	C\$ £m	Euro £m	Other £m	2019 Total £m	UK £m	US\$ £m	C\$ £m	Euro £m	Other £m	2018 Total £m
Cash at bank	6.2	4.8	0.3	6.8	3.4	21.5	4.7	4.3	1.1	2.9	1.6	14.6
Short term deposits	–	1.7	3.5	–	0.3	5.5	16.0	4.1	1.0	–	0.3	21.4
	6.2	6.5	3.8	6.8	3.7	27.0	20.7	8.4	2.1	2.9	1.9	36.0

The short term deposits and cash at bank are both interest bearing at rates linked to the UK base rate, or equivalent rate.

19. Financial instruments

The Group's overall management of the financial risks is carried out by a central treasury team under policies and procedures which are reviewed and approved by the Board. The treasury team identifies, evaluates and where appropriate, hedges financial risks in close cooperation with the Group's operating businesses. The treasury team does not undertake speculative foreign exchange dealings for which there is no underlying exposure.

The Group's principal financial instruments, other than a number of forward foreign currency contracts, comprise cash and short term deposits, investments, trade and other receivables and trade and other payables, borrowings and other liabilities. Trade and other receivables and trade and other payables arise directly from the Group's day-to-day operations.

The impact on the consolidated financial statements of adopting IFRS9 on the Group's financial instruments is not material and is described in the Group Accounting Policies section.

The financial risks to which the Group is exposed are those of credit, liquidity, foreign currency, interest rate and capital management. An explanation of each of these risks, how the Group manages these risks and an analysis of sensitivities is set out below and on page 31 within Internal Control and Risk Management, all of which have been audited.

a) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations; this arises principally from the Group's trade and other receivables from customers and from cash balances (including deposits) held with financial institutions.

The Group is exposed to customers ranging from government backed agencies and large public and private wholesalers, to small privately owned businesses and the underlying local economic risks vary throughout the world. Trade receivable exposures are managed locally in the operating units where they arise and credit limits are set as deemed appropriate for each customer.

The Group establishes a loss allowance that represents its estimate of potential losses in respect of specific trade and other receivables where it is deemed that a receivable may not be recoverable (see below). When the receivable is deemed irrecoverable, the provision is written off against the underlying receivable. During the year, the Group had no significant unrecoverable trade receivables.

Exposure to counterparty credit risk with financial institutions is controlled by the Group treasury team which establishes and monitors counterparty limits. Centrally managed funds are invested entirely with counterparties whose credit rating is "AA" or better. There are no significant concentrations of credit risk. There has been no historical or expected credit loss on cash and cash equivalents.

The Group's maximum exposure to credit risk was as follows:

	Carrying amount	
	2019 £m	2018 £m
Trade receivables	80.8	70.8
Other receivables	3.7	3.5
Cash and cash equivalents	27.0	36.0
	111.5	110.3

There is no material difference between the book value of the financial assets and their fair value at each reporting date. An analysis of the ageing and currency of trade receivables and the associated loss allowance is set out in note 16. An analysis of cash and cash equivalents is set out in note 18.

Impairment of financial assets

The Group applies the IFRS9 simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade receivables and accrued income.

The expected loss rates are based on the payment profiles of revenues over a period of 60 months ended 30 September 2019 and the corresponding historical credit losses experienced within this period. The historical loss rates are adjusted to reflect current and forward-looking information about macroeconomic factors affecting the ability of the customers to settle the receivables.

The Group has identified the current health of the economy (such as market interest rates and growth rates), of the countries in which it sells its goods to be the most relevant factors and accordingly adjusts the historical loss rates based on expected changes in these factors. An increase in credit risk is presumed if a debtor is more than 30 days past due in making a contractual payment. Where objective evidence exists that a trade receivable balance may be impaired, provision is made for the difference between its carrying amount and the present value of the estimated cash that will be recovered.

Evidence of impairment may include such factors as a change in credit risk profile of the customer, the customer being in default on a contract, or the customer entering insolvent administration proceedings. All significant balances are reviewed individually on a monthly basis for evidence of impairment.

The impact of applying the expected credit loss model does not materially impact the Group's provision for impaired assets given the quality and short term nature of the Group's trade receivables. As the impact of adopting IFRS9 is not material, the Group has not restated the prior year balances on adoption.

Notes to the Consolidated Financial Statements continued

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19. Financial instruments continued

b) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group continually monitors net cash and forecasts cash flows to ensure that sufficient resources are available to meet the Group's requirements in the short, medium and long term. Additionally, compliance with debt covenants is monitored regularly and during 2019 all covenants were complied with fully.

The Group is highly cash generative and uses monthly cash flow forecasts to monitor cash requirements and to optimise its return on shorter term deposits. Typically the Group ensures that it has sufficient cash on hand to meet foreseeable operational expenses, but the Group also maintains a committed multi-currency revolving facility of £30.0m. In May 2019, the Group formally extended this facility for a further two years to 1 June 2022. The facility has an accordion option to increase the committed facility by a further £30.0m up to a maximum of £60.0m. At 30 September 2019, the Group had utilised £6.1m of this facility (2018: £Nil). Interest on this facility is payable between 70–115bps over LIBOR, depending on the ratio of net debt to EBITDA.

On 8 July 2019, the Group extended its facilities with a new two-year term loan for an aggregate principal amount of £40.0m which was fully drawn to assist with the funding of the acquisition of VSP Technologies. At 30 September 2019, the Group had £36.0m of this loan outstanding, which is repayable in full by 7 July 2021. Interest on this facility is payable between 90–135bps over LIBOR, depending on the ratio of net debt to EBITDA.

The undrawn committed facilities available at 30 September are as follows:

	2019 £m	2018 £m
Expiring within one year	–	–
Expiring after one year	23.9	30.0

The Group's financial liabilities are as follows:

	Carrying amount	
	2019 £m	2018 £m
Trade payables	54.0	48.3
Other payables	5.4	3.6
Other liabilities (note 20)	11.3	5.6
	70.7	57.5

The maturities of the undiscounted financial liabilities are as follows:

Less than one year	70.6	57.5
One to two years	0.7	–
Two to five years	–	–
	71.3	57.5
Less: discount	(0.6)	–
	70.7	57.5

There is no material difference between the book value of these financial liabilities and their fair value at each reporting date.

c) Currency risk

The Group's principal currency risk comprises translational and transactional risk from its exposure to movements in US dollars, Canadian dollars and Euros. The transactional exposure arises on trade receivables, trade payables and cash and cash equivalents and these balances are analysed by currency in notes 16, 17 and 18, respectively.

The Group holds forward foreign exchange contracts for certain of the Group's businesses to hedge forecast transactional exposure to movements, primarily in the US dollar and Euro. These forward foreign exchange contracts are classified as cash flow hedges and are stated at fair value. The notional value of forward contracts as at 30 September 2019 was £39.5m (2018: £39.7m). The net fair value of forward foreign exchange contracts used as hedges at 30 September 2019 was a £0.4m asset (2018: £0.7m asset). The amount removed from Other Comprehensive Income and taken to the Consolidated Income Statement in cost of sales during the year was a £0.7m charge (2018: £0.9m credit). The change in the fair value of cash flow hedges taken to Other Comprehensive Income during the year was a £0.4m credit (2018: £0.7m credit).

Management considers that the most significant foreign exchange risk relates to the US dollar, Canadian dollar and Euro. The Group's sensitivity to a 10% strengthening in UK sterling against each of these currencies (with all other variables held constant) is as follows:

	2019 £m
Decrease in adjusted operating profit (at average rates)	
US dollar: UK sterling	2.7
Canadian dollar: UK sterling	2.1
Euro: UK sterling	1.2
Decrease in total equity (at spot rates)	
US dollar: UK sterling	3.4
Canadian dollar: UK sterling	7.2
Euro: UK sterling	2.5

19. Financial instruments continued**d) Interest rate risk**

Interest rate risk is the risk that changes in interest rates will affect the Group's results. The Group's interest rate risk arises primarily from its cash funds and borrowings. The Group does not undertake any hedging of interest rates. All cash deposits, held in the UK and overseas, are held on a short term basis at floating rates or overnight rates, based on the relevant UK base rate, or equivalent rate. Surplus funds are deposited with commercial banks that meet the credit criteria approved by the Board, for periods of between one and six months at rates that are generally fixed by reference to the relevant UK base rate, or equivalent rate. An increase of 1% in interest rates would not have a significant impact on the Group's profit before tax. An analysis of cash and cash equivalents at the reporting dates is set out in note 18.

e) Fair values

There are no material differences between the book value of financial assets and liabilities and their fair value. The basis for determining fair values are as follows:

Derivatives

Forward exchange contracts are designated as level 2 assets (in the "fair value hierarchy") and valued at year end forward rates, adjusted for the forward points to the contract's value date with gains and losses taken to equity. No contract's maturity date is greater than 18 months from the year end.

Trade and other receivables/payables

As the majority of receivables/payables have a remaining life of less than one year, the book value is deemed to reflect the fair value.

Other liabilities

The carrying amount represents a discounted value of the expected liability which is deemed to reflect the fair value.

f) Capital management risk

The Group's capital structure comprises retained reserves (£279.4m), cash funds (£27.0m) and medium term bank borrowing facilities (£53.9m undrawn as at 30 September 2019). The Group's objective when managing capital is to safeguard its ability to continue as a going concern and to maintain robust capital ratios to support the development of the business and provide strong returns to shareholders.

In order to maintain or adjust the capital structure, the Group may change the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or increase bank borrowings.

20. Other liabilities

	2019 £m	2018 £m
Future purchases of minority interests	4.3	4.5
Deferred consideration	7.0	1.1
	11.3	5.6
Analysed as:		
Due within one year	10.8	5.6
Due after one year	0.5	-

The movement in the liability for future purchases of minority interests is as follows:

	2019 £m	2018 £m
At 1 October	4.5	6.1
Acquisition of minority interest on exercise of options	-	(2.0)
Unwinding of discount	-	0.2
Fair value remeasurements	(0.2)	0.2
At 30 September	4.3	4.5

At 30 September 2019, the Group retained put options to acquire minority interests of 10% held in each of M Seals and Kentek which were both exercisable from November 2018. At 30 September 2019, the estimate of the financial liability to acquire the outstanding minority shareholdings was reassessed by the Directors, based on their current estimate of the future performance of these businesses and to reflect foreign exchange rates at 30 September 2019. This led to a remeasurement of the fair value of these put options and the liability was decreased by £0.2m (2018: £0.2m increase) reflecting a revised estimate of the future performance of these businesses. There is no charge from unwinding the discount on the liability (2018: £0.2m). In aggregate, £0.2m (2018: debit £0.4m) has been credited to the Consolidated Income Statement in respect of this remeasurement of the liability.

Deferred consideration comprises the following:

	Gross £m	Discount £m	Unwind £m	Exchange £m	2019 £m	2018 £m
VSP Technologies	5.6	(0.5)	0.1	0.1	5.3	-
DMR Seals	0.6	-	-	-	0.6	-
Sphere	1.3	(0.2)	-	-	1.1	-
Coast	-	-	-	-	-	0.1
FS Cables	-	-	-	-	-	1.0
At 30 September	7.5	(0.7)	0.1	0.1	7.0	1.1

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

20. Other liabilities continued

The amounts outstanding at 30 September 2019 are expected to be paid within the next two years and are based on the performance of these businesses in the period following their acquisition by the Group.

During the year, outstanding deferred consideration of £1.1m was paid to the vendors of FS Cables (£1.0m) and the vendor of Coast (£0.1m).

21. Minority interests

	£m
At 1 October 2018	4.8
Minority interest contribution	0.3
Share of minority net assets acquired of TPD	(2.5)
Share of profit	0.6
Dividends paid	(0.2)
Exchange adjustment	0.1
At 30 September 2018	3.1
Minority interest contribution	-
Share of profit	0.5
Dividends paid	(0.3)
Exchange adjustments	-
At 30 September 2019	3.3

External shareholders, represented by management in each business hold a 10% minority interest in M Seals and Kentek.

22. Acquisition of businesses

On 12 October 2018, the Group completed the acquisition of Actios SAS, the parent company of the Gremtek group ("Gremtek") of companies. The consideration was £6.9m net of cash acquired of £2.9m and includes acquisition expenses of £0.1m.

On 9 July 2019, the Group acquired the trade and net assets of Virginia Sealing Products Inc ("VSP Technologies"), based in Virginia US, for initial cash consideration of £57.2m, which is net of cash acquired of £0.8m and includes £1.2m of acquisition expenses. Deferred consideration of £5.1m (£5.6m undiscounted) is assumed to be payable based on the operating profit achieved in the 12 months ending 30 June 2020.

On 2 September 2019, the Group acquired DMR Seals (Holdings) Limited and DMR Gaskets Limited ("DMR Seals") for initial consideration of £7.3m which included surplus cash of £0.3m and acquisition expenses of £0.1m. Deferred consideration of £0.6m is assumed to be payable based on the operating profit achieved in the 12 months ending 30 April 2020.

On 20 September 2019, the Group acquired Sphere Surgical Pty Limited and Aspire Surgical Pty Limited (together "Sphere") for £6.6m net of cash acquired of £0.1m and including acquisition expenses of £0.1m. Deferred consideration of £1.1m (£1.3m undiscounted) is assumed to be payable based on gross profit achieved in the 12 months ending 30 June 2020 and 2021.

Set out below is an analysis of the net book values and fair values relating to these acquisitions:

	VSP Technologies		Others		Total	
	Book value £m	Fair value £m	Book value £m	Fair value £m	Book value £m	Fair value £m
Acquisition intangible assets	-	40.0	-	13.2	-	53.2
Deferred tax	-	-	-	(3.3)	-	(3.3)
Property, plant and equipment	1.4	0.5	0.6	0.3	2.0	0.8
Inventories	3.2	3.2	2.1	1.8	5.3	5.0
Trade and other receivables	5.5	5.2	3.1	3.0	8.6	8.2
Trade and other payables	(2.5)	(2.5)	(2.9)	(3.0)	(5.4)	(5.5)
Net assets acquired	7.6	46.4	2.9	12.0	10.5	58.4
Goodwill	-	14.7	-	9.4	-	24.1
	7.6	61.1	2.9	21.4	10.5	82.5
Cash paid		56.8		23.4		80.2
Cash acquired		(0.8)		(3.7)		(4.5)
Expenses of acquisition		1.2		0.3		1.5
Net cash paid, after acquisition expenses		57.2		20.0		77.2
Deferred consideration payable (note 20)		5.1		1.7		6.8
Less: expenses of acquisition		(1.2)		(0.3)		(1.5)
Total consideration		61.1		21.4		82.5

The fair values set out above are provisional and will be finalised in the next financial year. Goodwill of £24.1m recognised on these acquisitions represents the amount paid for future sales growth from both new customers and new products, operating cost synergies and employee know-how.

22. Acquisition of businesses continued

From the date of acquisition, each acquired business contributed the following to Group revenue and adjusted operating profit:

	Date of acquisition	Revenue (£m)	Adjusted operating profit ¹ (£m)
Gremtek	12 Oct 2018	10.0	1.5
VSP Technologies	9 Jul 2019	9.0	1.6
DMR Seals	2 Sep 2019	0.3	0.1
Sphere	20 Sep 2019	0.1	0.1
Contribution in year		19.4	3.3
Extrapolated for 12 months ²		38.3	8.3
Pro forma for year ended 30 September 2019		57.7	11.6

1 After appropriate allocation of head office costs.

2 Pro forma revenue and adjusted operating profit has been extrapolated from the results reported since acquisition to indicate what these businesses would have contributed if they had been acquired at the beginning of the financial year on 1 October 2018. These amounts should not be viewed as confirmation of the results of these businesses that would have occurred, if these acquisitions had been completed at the beginning of the year.

The Group's pro forma adjusted operating profit of £105.5m (note 3) comprises the Group's adjusted operating profit of £97.2m and the pro forma adjusted operating profit of £8.3m relating to these acquired businesses.

23. Reconciliation of operating profit to cash flow from operating activities

	2019 £m	2019 £m	2018 £m	2018 £m
Operating profit		84.1		73.2
Acquisition related charges (note 11)		13.1		9.6
CEO transition costs		–		2.1
Adjusted operating profit		97.2		84.9
CEO transition costs paid		(1.3)		(0.8)
		95.9		84.1
Depreciation or amortisation of tangible and other intangible assets	5.4		4.8	
Share-based payments expense (note 5)	0.8		1.0	
Defined benefit pension scheme (note 25)	(0.4)		(0.5)	
Non-cash items		5.8		5.3
Operating cash flow before changes in working capital		101.7		89.4
Increase in inventories	(12.2)		(8.3)	
Increase in trade and other receivables	(1.2)		(5.2)	
Increase in trade and other payables	4.0		8.4	
Increase in working capital		(9.4)		(5.1)
Cash flow from operating activities, before acquisition expenses		92.3		84.3

24. (Net debt)/cash funds

The movement in net funds during the year is as follows:

	1 Oct 2018 £m	Cash flow £m	Exchange movements £m	Non-cash movements £m	30 Sep 2019 £m
Cash and cash equivalents	36.0	(10.8)	1.8	–	27.0
Borrowings	–	(41.1)	(0.7)	(0.3)	(42.1)
Cash funds/(net debt)	36.0	(51.9)	1.1	(0.3)	(15.1)
	1 Oct 2017 £m	Cash flow £m	Exchange movements £m	Non-cash movements £m	30 Sep 2018 £m
Cash and cash equivalents	22.3	13.1	0.6	–	36.0
Borrowings	–	–	–	–	–
Cash funds	22.3	13.1	0.6	–	36.0

The non-cash movements in the year ended 30 September 2019 reflect accrued interest in excess of interest paid.

The Group has a committed multi-currency revolving facility of £30.0m. In May 2019, the Group formally extended this facility for a further two years to 1 June 2022. The facility has an accordion option to increase the committed facility by a further £30.0m up to a maximum of £60.0m. At 30 September 2019, the Group had utilised £6.1m of this facility (2018: £Nil). Interest on this facility is payable between 70–115bps over LIBOR, depending on the ratio of net debt to EBITDA.

On 8 July 2019, the Group extended its facilities with a new two-year term loan for an aggregate principal amount of £40.0m which was fully drawn to assist with the funding of the acquisition of VSP Technologies. At 30 September 2019, the Group had £36.0m of this loan outstanding, which is repayable in full by 7 July 2021. Interest on this facility is payable between 90–135bps over LIBOR, depending on the ratio of net debt to EBITDA.

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

25. Retirement benefit obligations

The Group maintains two pension arrangements which are accounted for under IAS19 (*Revised*) (*Employee Benefits*). The principal arrangement is the defined benefit pension scheme in the UK, maintained by Diploma Holdings PLC and called the Diploma Holdings PLC UK Pension Scheme ("the Scheme"). This Scheme provides benefits based on final salary and length of service on retirement, leaving service or death and has been closed to further accrual since 5 April 2000.

The second and smaller pension arrangement is operated by Kubo, a business based in Switzerland and provides benefits on retirement, leaving service or death for the employees of Kubo in accordance with Swiss law. The Kubo pension scheme is a defined contribution based scheme, which for technical reasons, is required under IFRS to be accounted for in accordance with IAS19 (revised).

The amount of pension deficit included in the Consolidated Statement of Financial Position in respect of these two pension arrangements is:

	2019 £m	2018 £m
Diploma Holdings PLC UK Pension Scheme	12.0	6.8
Kubo Pension Scheme	5.8	3.7
Pension scheme net deficit	17.8	10.5

The amounts included in the Consolidated Income Statement in respect of these two pension arrangements are:

	2019 £m	2018 £m
Diploma Holdings PLC UK Pension Scheme	(0.3)	(0.1)
Kubo Pension Scheme	(0.4)	(0.2)
Amounts charged to the Consolidated Income Statement	(0.7)	(0.3)

Defined contribution schemes operated by the Group's businesses are not included in these disclosures.

Diploma Holdings PLC UK Pension Scheme

The Scheme is subject to a Statutory Funding Objective under the Pensions Act 2004 which requires that a valuation of the Scheme is carried out at least once every three years to determine whether the Statutory Funding Objective is met. As part of the process the Company must agree with the Trustees of the Scheme the contributions to be paid to address any shortfall against the Statutory Funding Objective. The most recent triennial actuarial valuation carried out as at 30 September 2016 reported that the Scheme had a funding deficit of £9.2m and held assets which covered 75% of its liabilities at that date. The next triennial actuarial valuation of the Scheme will be carried out as at 30 September 2019 and the results of the valuation will be reported in the 2020 Annual Report & Accounts. There were no Scheme amendments, curtailments or settlements during the year.

On 28 September 2018, the Trustees completed a Buy-In of the pensioner liabilities in the Scheme with Just Retirement Limited. The Scheme paid £12.3m to Just Retirement Limited on 28 September 2018 to fund 95% of the Buy-In premium and £0.7m was paid on 22 October 2018 to fund the remaining 5% of the premium. The impact of this transaction has been reflected in the pension disclosures set out below.

The Scheme is managed by a set of Trustees appointed in part by the Company and in part from elections by members of the Scheme. The Trustees have responsibility for obtaining valuations of the fund, administering benefit payments and investing the Scheme's assets. The Trustees delegate some of these functions to their professional advisors where appropriate.

The Scheme exposes the Company and therefore the Group, to a number of risks:

- **Investment risk.** The Scheme holds investments in asset classes, such as equities, which have volatile market values and while these assets are expected to provide real returns over the long term, volatility over the short term can cause additional funding to be required if a deficit emerges.
- **Interest rate risk.** The Scheme's liabilities are assessed using market yields on high quality corporate bonds to discount the liabilities. As the Scheme's assets include equities, the value of the assets and liabilities may not move in the same way.
- **Inflation risk.** A significant proportion of the benefits under the Scheme are linked to inflation. The Scheme's assets are expected to provide a good hedge against inflation over the long term, however movements over the short term could lead to funding deficits emerging.
- **Mortality risk.** In the event that members live longer than assumed, a larger funding deficit may emerge in the Scheme.

a) Pension deficit included in the Consolidated Statement of Financial Position

	2019 £m	2018 £m
Market value of Scheme assets:		
Equities ¹	19.3	20.0
Buy-In policy ²	11.3	9.5
Cash	0.1	–
	30.7	29.5
Present value of Scheme liabilities	(42.7)	(36.3)
Pension scheme net deficit	(12.0)	(6.8)

¹ Quoted market price in an active market.

² The Buy-In policy was valued on the same basis as the underlying pensioner liabilities.

In addition to the Buy-In policy, the pension scheme net deficit includes £3.5m of historic annuities and related assets on a net basis, rather than on a gross basis.

25. Retirement benefit obligations continued

b) Amounts charged to the Consolidated Income Statement

	2019 £m	2018 £m
Charged to operating profit	(0.1)	–
Interest cost on liabilities	(1.0)	(1.0)
Interest on assets	0.8	0.9
Charged to financial expense, net (note 6)	(0.2)	(0.1)
Amounts charged to the Consolidated Income Statement	(0.3)	(0.1)

c) Amounts recognised in the Consolidated Statement of Comprehensive Income

	2019 £m	2018 £m
Investment gain/(loss) on Scheme assets in excess of interest	1.8	(1.8)
Effect of changes in financial assumptions on Scheme liabilities	(7.2)	0.6
Effect of changes in demographic assumptions on Scheme liabilities	–	(0.6)
Experience adjustments on Scheme liabilities	–	–
Actuarial (losses) charged in the Consolidated Statement of Comprehensive Income	(5.4)	(1.8)

The cumulative amount of actuarial losses recognised in the Consolidated Statement of Comprehensive Income, since the transition to IFRS, is £13.0m (2018: £7.6m).

d) Analysis of movement in the pension deficit

	2019 £m	2018 £m
At 1 October	6.8	5.4
Amounts charged to the Consolidated Income Statement	0.3	0.1
Contributions paid by employer	(0.5)	(0.5)
Net effect of remeasurements of Scheme assets and liabilities	5.4	1.8
At 30 September	12.0	6.8

e) Analysis of movements in the present value of the Scheme liabilities

	2019 £m	2018 £m
At 1 October	36.3	36.3
Past service cost	0.1	–
Interest cost on liabilities	1.0	1.0
Impact from changes in actuarial assumptions	7.2	–
Benefits paid	(1.9)	(1.0)
At 30 September	42.7	36.3

f) Analysis of movements in the present value of the Scheme assets

	2019 £m	2018 £m
At 1 October	29.5	30.9
Interest on assets	0.8	0.9
Return on Scheme assets	1.8	(1.8)
Contributions paid by employer	0.5	0.5
Benefits paid	(1.9)	(1.0)
At 30 September	30.7	29.5

The actual return on the Scheme assets during the year was a gain of £2.6m (2018: £0.9m loss).

Assets

The Scheme's assets are held in passive unit funds managed by Legal & General Investment Management and at 30 September 2019, the major categories of assets were as follows:

	2019 %	2018 %
North America equities	16	17
UK equities	16	17
European equities (non-UK)	16	17
Asia-Pacific and Emerging Markets equities	16	17
Buy-In policy	36	32

Notes to the Consolidated Financial Statements continued

For the year ended 30 September 2019

25. Retirement benefit obligations continued

Principal actuarial assumptions for the Scheme at balance sheet dates

		2019 %	2018 %	2017 %	2016 %
Inflation rate	– RPI	3.4	3.4	3.4	3.2
	– CPI	2.4	2.4	2.4	2.4
Expected rate of pension increases	– CPI	2.4	2.4	2.4	2.4
Discount rate		1.8	2.9	2.8	2.3

Demographic assumptions

Mortality table used:	S2NA
Year the mortality table was published:	CMI 2017
Allowance for future improvements in longevity:	Year of birth projections, with a long term improvement rate of 1.0%
Allowance made for members to take a cash lump sum on retirement:	Members are assumed to take 100% of their maximum cash sum (based on current commutation factors)
The weighted average duration of the defined benefit obligation is around 18 years	

Sensitivities

The sensitivities of the 2019 pension liabilities to changes in assumptions are as follows:

Factor	Assumption	Impact on pension liabilities	
		Estimated increase %	Estimated increase £m
Discount rate	Decrease by 0.5%	9.1	3.9
Inflation	Increase by 0.5%	4.2	1.8
Life expectancy	Increase by one year	3.3	1.4

Risk mitigation strategies

When setting the investment strategy for the Scheme, the Trustees, in conjunction with the employer, take into account the liability profile of the Scheme. The current strategy is designed to invest in growth assets in respect of deferred pensioners. Annuity policies have been taken out in respect of some historic pensioners, but the Scheme has not purchased annuities for retirements since 2005.

In addition to these individual annuity policies, the Trustees have purchased a Buy-In policy for all existing pensioners as at 1 September 2018. The Buy-In policy secures the Scheme against both market and mortality risk relating to these pensioners. The Scheme however remains liable ultimately for the liabilities, should the insurance company which sold the liabilities go into insolvent liquidation.

Effect of the Scheme on the Group's future cash flows

The Company is required to agree a schedule of contributions with the Trustees of the Scheme following each triennial actuarial valuation. Following the triennial actuarial valuation carried out as at 30 September 2016, the Company agreed to contribute £0.5m in cash to the scheme annually. The next valuation of the Scheme will be carried out as at 30 September 2019.

The Kubo Pension Scheme ("the Kubo Scheme")

In accordance with Swiss law, Kubo's pension benefits are contribution based with the level of benefits varying according to category of employment. Swiss law requires certain guarantees to be provided on such pension benefits. Kubo finances its Swiss pension benefits through the ASGA Pensionskasse, a multi-employer plan of non-associated companies which pools risks between participating companies. As at 30 September 2019, the ASGA Pensionskasse had a local coverage ratio of 108.1%. Set out below is a summary of the key features of the Kubo Scheme.

a) Pension deficit included in the Consolidated Statement of Financial Position

	2019 £m	2018 £m
Assets of the Kubo Scheme ¹	8.8	9.1
Actuarial liabilities of the Kubo Scheme	(14.6)	(12.8)
Pension scheme net deficit	(5.8)	(3.7)

¹ The assets of the Kubo Scheme are held as part of the employee funds managed by ASGA Pensionskasse.

b) Amounts charged to the Consolidated Income Statement

	2019 £m	2018 £m
Service cost	(0.4)	(0.2)
Amount charged to operating profit in the Consolidated Income Statement	(0.4)	(0.2)

c) Analysis of movement in the pension deficit

	2019 £m	2018 £m
At 1 October	3.7	4.5
Amounts charged to the Consolidated Income Statement	0.4	0.2
Contributions paid by employer	(0.4)	(0.2)
Net effect of remeasurements of Kubo Scheme assets and liabilities	1.8	(0.8)
Exchange adjustments	0.3	–
At 30 September	5.8	3.7

25. Retirement benefit obligations continued

d) Amounts recognised in the Consolidated Statement of Comprehensive Income

The actuarial loss charged to the Consolidated Statement of Comprehensive Income is £1.8m (2018: £0.8m gain).

Principal actuarial assumptions for the Kubo Scheme at balance sheet dates

	2019	2018
Expected rate of pension increase	0%	0%
Expected rate of salary increase	1.0%	1.0%
Discount rate	0.0%	1.0%
Interest credit rate	0.5%	1.0%
Mortality	BVG2015	BVG2015

Sensitivities

The sensitivities of the 2019 pension liabilities to changes in assumptions are as follows:

Factor	Assumption	Impact on pension liabilities	
		Estimated increase %	Estimated increase £m
Discount rate	Decrease by 0.25%	5.4	0.8
Life expectancy	Increase by one year	2.7	0.4

Effect of the Kubo Scheme on the Group's future cash flows

	£m
Best estimate of employer's contribution in 2020	0.4
Best estimate of employees' contribution in 2020	0.4

The weighted average duration of the defined benefit obligation is approximately 20 years.

26. Commitments

At 30 September 2019, the Group had outstanding aggregate commitments for future lease payments (under non-cancellable operating leases) in respect of the following years:

	Land and buildings		Other		Total	
	2019 £m	2018 £m	2019 £m	2018 £m	2019 £m	2018 £m
Within one year	6.1	4.4	1.5	1.5	7.6	5.9
For years two to five	17.9	11.1	2.3	2.1	20.2	13.2
After five years	11.5	5.0	–	–	11.5	5.0
	35.5	20.5	3.8	3.6	39.3	24.1

Other commitments comprise plant and machinery, motor vehicles and office equipment. Operating lease payments made during the year in respect of land and buildings and other commitments were £5.4m (2018: £4.6m) and £1.9m (2018: £1.6m), respectively.

27. Auditor's remuneration

During the year the Group paid fees for the following services from the auditor:

	2019 £m	2018 £m
Fees payable to the auditor for the audit of:		
– the Company's Annual Report & Accounts	0.1	0.1
– the Company's subsidiaries	0.6	0.5
Audit fees	0.7	0.6

Non-audit fees of £18,000 (2018: £15,000) were paid to the Group's auditor for carrying out "agreed upon procedures" on both the Half Year Announcement (which is unaudited) and on certifying financial information for a subsidiary.

28. Exchange rates

The exchange rates used to translate the results of the overseas businesses are as follows:

	Average		Closing	
	2019	2018	2019	2018
US dollar (US\$)	1.27	1.35	1.23	1.30
Canadian dollar (C\$)	1.69	1.73	1.63	1.69
Euro (€)	1.13	1.13	1.13	1.12
Swiss franc (CHF)	1.27	1.31	1.23	1.27
Australian dollar (A\$)	1.81	1.78	1.83	1.80

Group Accounting Policies

For the year ended 30 September 2019

The consolidated financial statements have been prepared in accordance with IFRS as endorsed by the EU and in accordance with the Companies Act 2006, as applicable to companies reporting under IFRS. The accounting policies set out below have been consistently applied in 2019 and the comparative year.

There were no new standards, amendments or interpretations to existing standards which have been published and endorsed by the EU and which have a significant impact on the results, financial position or presentation of the consolidated financial statements for the year ended 30 September 2019.

1.1 Basis of preparation

The consolidated financial statements have been prepared under the historical cost convention, except for derivative financial instruments which are held at fair value. The consolidated financial statements have been prepared on a going concern basis, as discussed on page 61.

1.2 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries and Employee Benefit Trust ("EBT")). Control exists when the Company is exposed or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The assets, liabilities and results of subsidiaries acquired or disposed of during the year are included in the Consolidated Income Statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those detailed herein to ensure that the Group financial statements are prepared on a consistent basis. All intra-Group transactions, balances, income and expenses are eliminated in preparing the consolidated financial statements.

Non-controlling interests, defined as minority interests, in the net assets of consolidated subsidiaries are identified separately from the Group's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination.

1.2.a. New accounting standards adopted

IFRS15 (Revenue from contracts with customers)

IFRS15 replaces IAS18 and introduces a single, principles-based approach to recognition and measurement of revenue from sales contracts with customers. The modified approach requires the identification of performance obligations in a sales contract and sets out when revenue is recognised based upon when those performance obligations have been met.

For the large majority of the Group's contracts, the performance obligation is when goods are made available, which under IFRS15 would be recognised at a single point of time, on delivery of the goods, consistent with the current accounting treatment under IAS18.

Within the Life Sciences Sector there are a small number of contracts where goods and services are delivered and there is more than one performance obligation; in the majority of instances revenue for these contracts was already being separately recognised prior to the adoption of IFRS15. Where revenue has been recognised for the delivery of goods, revenue recognition has been amended to ensure the element of revenue attributable to the service is separately recognised over time. The financial impact on revenues is not material and the Group has not restated the prior year comparative.

IFRS9 (Financial Instruments)

IFRS9 replaces IAS39 and concerns the classification, measurement and derecognition of financial assets and financial liabilities; introduces an expected credit loss model for the impairment of financial assets; and sets out changes to the hedge accounting relationships.

The adoption of this standard has not had a material impact on the Consolidated Statement of Financial Position, as the financial instruments are already being accounted for on the same measurement and valuation techniques as set out in IFRS9. All existing hedge relationships will continue to qualify for hedge accounting under IFRS9 and the Group has elected to continue to apply the hedge accounting requirements of IAS39, as allowed under IFRS9.

On transition to IFRS9 the measurement basis of the Group's financial assets and financial liabilities has not changed, aside from the Group's investments (see 1.14 for further detail).

The Group has adopted the simplified approach to provide for losses on receivables within the scope of IFRS9. The impact of applying the expected credit loss model is not material given the quality and short term nature of the Group's trade receivables. As the impact of adopting IFRS9 is not material, the Group has not restated the prior period on adoption.

1.3 Acquisitions

Acquisitions are accounted for using the acquisition method as at the acquisition date, which is the date on which control is transferred to the Group. Goodwill at the acquisition date represents the cost of the business combination (excluding acquisition related costs, which are expensed as incurred) plus the amount of any non-controlling interest in the acquiree in excess of the fair value of the identifiable tangible and intangible assets, liabilities and contingent liabilities acquired.

Minority interests may be initially measured at fair value or, alternatively, at the minority interest's proportionate share of the recognised amounts of the acquiree's identifiable net assets. The choice of measurement basis is made for each business combination separately.

1.4 Divestments

The results and cash flows of major lines of businesses that have been divested have been classified as discontinued businesses. There were no discontinued operations in either 2019 or 2018.

1.5 Revenue recognition

Revenue is measured as the fair value of the consideration received or receivable for goods and services supplied to customers, after deducting sales allowances and value-added taxes; revenue receivable for services supplied to customers, as opposed to goods, is less than ca. 3% of Group revenue. Under IFRS15, each customer contract is assessed to identify the performance obligation. An assessment of the timing of revenue recognition is made for each performance obligation. Revenue is recognised at a point in time for all standard revenue transactions when control of the goods provided is transferred to the customer. Revenue is also recognised at a point in time for contracts that contain multiple elements ("service contracts") when the agreed output is produced by the customer, unless there are specific performance obligations to deliver other services over time. The revenue on such service contracts is not material.

The transaction price is allocated to each performance obligation based on the relative stand-alone selling prices of the goods or services provided. If a stand-alone selling price is not available, the Group will estimate the selling price with reference to the price that would be charged for the goods or services if they were sold separately. There are no contracts with variable consideration.

Provision is made for returns and in the few instances where rebates are provided. The impact on transition is not material. There are no capitalised contract costs recognised by the Group.

1.6 Employee benefits

The Group operates a number of pension plans, both of the defined contribution and defined benefit type.

- Defined contribution pension plans: Contributions to the Group's defined contribution schemes are recognised as an employee benefit expense when they fall due.
- Defined benefit pension plan: The deficit recognised in the balance sheet for the Group's defined benefit pension plan is the present value of the defined benefit obligation at the balance sheet date

less the fair value of the scheme assets. The defined benefit obligation is calculated by independent actuaries using the projected unit cost method and by discounting the estimated future cash flows using interest rates on high-quality corporate bonds. The pension expense for the Group's defined benefit plan is recognised as follows:

- i) Within the Consolidated Income Statement:
 - Service cost of current members of the Kubo Scheme.
 - Gains and losses arising on settlements and curtailments – where the item that gave rise to the settlement or curtailment is recognised in operating profit.
 - Interest cost on the net deficit in the plan – calculated by applying the discount rate to the net defined benefit liability at the start of the annual reporting period.
- ii) Within the Consolidated Statement of Comprehensive Income (“Other Comprehensive Income”):
 - Actuarial gains and losses arising on the assets and liabilities of the plan related to actual experience and any changes in assumptions at the end of the year.
- c) Share-based payments: Equity-settled transactions (which are where the Executive Directors and certain senior employees receive a part of their remuneration in the form of shares in the Company, or rights over shares) are measured at fair value at the date of grant. The fair value determined at the grant date takes account of the effect of market based measures, such as Total Shareholder Return (“TSR”) targets upon which vesting of part of the award is conditional and is expensed to the Consolidated Income Statement on a straight-line basis over the vesting period, with a corresponding credit to equity. The cumulative expense recognised is adjusted to take account of shares forfeited by Executives who leave during the performance or vesting period and, in the case of non-market related performance conditions, where it becomes unlikely that shares will vest. For the market-based measure, the Directors have used a predicted future value model to determine fair value of the shares at the date of grant.

The Group operates an EBT for the granting of shares to Executives. The cost of shares in the Company purchased by the EBT are shown as a deduction from equity.

1.7 Foreign currencies

The individual financial statements of each Group entity are prepared in their functional currency, which is the currency of the primary economic environment in which that entity operates. For the purpose of the consolidated financial statements, the results and financial position of each entity are translated into UK sterling, which is the presentational currency of the Group.

- a) Reporting foreign currency transactions in functional currency: Transactions in currencies other than the entity's functional currency (foreign currencies) are initially recorded at the rates of exchange prevailing on the dates of the transactions. At each subsequent balance sheet date:
 - i) Foreign currency monetary items are retranslated at the rates prevailing at the balance sheet date. Exchange differences arising on the settlement or retranslation of monetary items are recognised in the Consolidated Income Statement.
 - ii) Non-monetary items measured at historical cost in a foreign currency are not retranslated.
 - iii) Non-monetary items measured at fair value in a foreign currency are retranslated using the exchange rates at the date the fair value was determined. Where a gain or loss on non-monetary items is recognised directly in equity, any exchange component of that gain or loss is also recognised directly in equity and conversely, where a gain or loss on a non-monetary item is recognised in the Consolidated Income Statement, any exchange component of that gain or loss is also recognised in the Consolidated Income Statement.
- b) Translation from functional currency to presentational currency: When the functional currency of a Group entity is different from the Group's presentational currency, its results and financial position are translated into the presentational currency as follows:
 - i) Assets and liabilities are translated using exchange rates prevailing at the balance sheet date.

- ii) Income and expense items are translated at average exchange rates for the year, except where the use of such an average rate does not approximate the exchange rate at the date of the transaction, in which case the transaction rate is used.
- iii) All resulting exchange differences are recognised in Other Comprehensive Income; these cumulative exchange differences are recognised in the Consolidated Income Statement in the period in which the foreign operation is disposed of.
- c) Net investment in foreign operations: Exchange differences arising on a monetary item that forms part of a reporting entity's net investment in a foreign operation are recognised in the Consolidated Income Statement in the separate financial statements of the reporting entity or the foreign operation as appropriate. In the consolidated financial statements such exchange differences are initially recognised in Other Comprehensive Income as a separate component of equity and subsequently recognised in the Consolidated Income Statement on disposal of the net investment.

1.8 Taxation

The tax expense relates to the sum of current tax and deferred tax.

Current tax is based on taxable profit for the year, which differs from profit before taxation as reported in the Consolidated Income Statement. Taxable profit excludes items of income and expense that are taxable (or deductible) in other years and also excludes items that are never taxable or deductible. The Group's liability for current tax, including UK corporation tax and overseas tax, is calculated using rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax is accounted for using the balance sheet liability method. Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Temporary differences arise primarily from the recognition of the deficit on the Group's defined benefit pension scheme, the difference between accelerated capital allowances and depreciation and for short term timing differences where a provision held against receivables or inventory is not deductible for taxation purposes. However, deferred tax assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit, nor the accounting profit.

Deferred tax liabilities are also recognised for taxable temporary differences arising on investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. No deferred tax is recognised on the unremitted earnings of overseas subsidiaries, as the Group controls the dividend policies of its subsidiaries.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled. Deferred tax is charged or credited to the Consolidated Income Statement, except when the item on which the tax or charge is credited or charged directly to equity, in which case the deferred tax is also dealt with in equity. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the assets to be recovered. Tax assets and liabilities are offset when there is a legally enforceable right to enforce current tax assets against current tax liabilities and when the deferred income tax relates to the same fiscal authority.

1.9 Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Cost comprises the purchase price plus costs directly incurred in bringing the asset into use. All repairs and maintenance expenditure is charged to the Consolidated Income Statement in the period in which it is incurred.

Group Accounting Policies continued

For the year ended 30 September 2019

Freehold land is not depreciated. Depreciation on other items of property, plant and equipment begins when the asset is available for use and is charged to the Consolidated Income Statement on a straight-line basis to write off the cost, less residual value of the asset, over its estimated useful life as follows:

Freehold property	– between 20 and 50 years
Leasehold property	– term of the lease
Plant and equipment	– plant and machinery between 3 and 7 years – IT hardware between 3 and 5 years – fixtures and fittings between 5 and 15 years
Hospital field equipment	– 5 years

The depreciation method used, residual values and estimated useful lives are reviewed and changed, if appropriate, at least at each financial year end. Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, over the term of the relevant lease. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses arising on disposals are determined by comparing sales proceeds with carrying amount and are recognised in the Consolidated Income Statement.

1.10 Intangible assets

All intangible assets, excluding goodwill arising on a business combination, are stated at their amortised cost or fair value at initial recognition less any provision for impairment.

a) Research and development costs

Research expenditure is written off as incurred. Development costs are written off as incurred unless forecast revenues for a particular project exceed attributable forecast development costs in which case they are capitalised and amortised on a straight-line basis over the asset's estimated useful life. Costs are capitalised as intangible assets unless physical assets, such as tooling, exist when they are classified as property, plant and equipment.

b) Computer software costs

Where computer software is not integral to an item of property, plant or equipment its costs are capitalised as other intangible assets. Amortisation is provided on a straight-line basis over its useful economic life of between three and seven years.

c) Acquired intangible assets – business combinations

Intangible assets that may be acquired as a result of a business combination, include, but are not limited to, customer lists, supplier lists, databases, technology and software and patents that can be separately measured at fair value, on a reliable basis, are separately recognised on acquisition at the fair value, together with the associated deferred tax liability. Amortisation is charged on a straight-line basis to the Consolidated Income Statement over the expected useful economic lives.

Fair values of customer and supplier relationships on larger acquisitions are valued using a discounted cash flow model; databases are valued using a replacement cost model. For smaller acquisitions, intangible assets are assessed using historical experience of similar transactions.

d) Goodwill – business combinations

Goodwill arising on the acquisition of a subsidiary represents the excess of the aggregate of the fair value of the consideration over the aggregate fair value of the identifiable intangible, tangible and current assets and net of the aggregate fair value of the liabilities (including contingent liabilities of businesses acquired at the date of acquisition). Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Transaction costs are expensed and are not included in the cost of acquisition.

1.11 Impairment of tangible and intangible assets

An impairment loss is recognised to the extent that the carrying amount of an asset or cash-generating unit ("CGU") exceeds its recoverable amount.

The recoverable amount of an asset or CGU is the higher of: (i) its fair value less costs to sell; and (ii) its value in use. Its value in use is the present value of the future cash flows expected to be derived from the asset or CGU, discounted using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU. Impairment losses are recognised immediately in the Consolidated Income Statement.

a) Impairment of goodwill

Goodwill acquired in a business combination is allocated to a CGU; CGUs for this purpose are the Group's three Sectors which represent the lowest level within the Group at which the goodwill is monitored by the Group's Board of Directors for internal and management purposes. CGUs to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired.

If the recoverable amount of the CGU is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the goodwill attributable to the CGU. Impairment losses cannot be subsequently reversed.

b) Impairment of other tangible and intangible assets

Other tangible and intangible assets are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. Impairment losses and any subsequent reversals are recognised in the Consolidated Income Statement.

1.12 Inventories

Inventories are stated at the lower of cost (generally calculated on a FIFO or weighted average cost basis depending on the nature of the inventory) and net realisable value, after making due allowance for any obsolete or slow moving inventory. Cost comprises direct materials, duty and freight-in costs.

Net realisable value represents the estimated selling price less all estimated costs of completion and the estimated costs necessary to make the sale.

1.13 Financial instruments

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

a) Trade receivables and loss allowance

Trade receivables are initially measured at fair value, do not carry any interest and are reduced by a charge for impairment for estimated irrecoverable amounts. Such impairment losses are recognised in the Consolidated Income Statement, calculated under IFRS9 (see note 1.2(a)).

b) Trade payables

Trade payables are non-interest bearing and are initially measured at their nominal value.

c) Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, interest bearing deposits, bank overdrafts and short term highly liquid investments with original maturities of three months or less that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value. Bank overdrafts are repayable on demand and can form an integral part of the Group's cash management. Bank overdrafts (where used) are presented net of cash and cash equivalents on the Balance sheet.

d) Put options held by minority interests

The purchase price of shares to be acquired under options held by minority shareholders in the Group's subsidiaries are calculated by reference to the estimated profitability of the relevant subsidiary at the time of exercise, using a multiple based formula. The net present value of the estimated future payments under these put options is shown

as a financial liability. The corresponding entry is recognised in equity as a deduction against retained earnings. At the end of each year, the estimate of the financial liability is reassessed and any change in value is recognised in the Consolidated Income Statement, as part of finance income or expense. Where the liability is in a foreign currency, any change in the value of the liability resulting from changes in exchange rates is recognised in the Consolidated Income Statement.

e) Derivative financial instruments and hedge accounting

The Group holds derivative financial instruments in the form of forward foreign exchange contracts to hedge its foreign currency exposure. These derivatives are designated as cash flow hedges. The Group has elected to continue to apply the hedge accounting requirements of IAS39, as allowed under IFRS9.

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and subsequent changes in the fair value of foreign currency derivatives which are designated and effective as hedges of future cash flows are recognised in equity in the hedging reserve and in Other Comprehensive Income and are reclassified to profit or loss on maturity of the derivative. Changes in the fair value of foreign currency derivatives which are ineffective or do not meet the criteria for hedge accounting in accordance with IAS39 are recognised immediately in the Consolidated Income Statement.

The Group documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedging transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items.

No derivative contracts have been designated as fair value hedges or net investment hedges.

f) Borrowings

Borrowings are initially recognised at the fair value of the consideration received. They are subsequently measured at amortised cost. Borrowings are classified as non-current when the repayment date is more than 12 months from the period end date or where they are drawn on a facility with more than 12 months to expiry.

1.14 Investments (fair value through Other Comprehensive Income)

The investment held by the Group comprises equity shares which are not held for the purposes of equity trading and in accordance with IFRS9 is classified as fair value through Other Comprehensive Income. They are initially recognised at fair value. Subsequent to initial recognition, they are measured at fair value and changes therein are recognised in Other Comprehensive Income.

1.15 Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risk and rewards of ownership to the lessee. Leases include hire purchase contracts which have characteristics similar to finance or operating leases. All other leases are classified as operating leases. Rentals payable under operating leases are charged to the Consolidated Income Statement on a straight-line basis over the term of the relevant lease. Benefits received and receivable as an incentive to enter into an operating lease are also spread on a straight-line basis over the expected lease term.

1.16 Other liabilities

Other liabilities are recognised when the Group has legal or constructive obligation as a result of a past event and it is probable that the Group will be required to settle that obligation. Other liabilities are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date.

1.17 Dividends

The annual final dividend is not provided for until approved at the AGM; interim dividends are charged in the period they are paid.

1.18 Share capital and reserves

Ordinary shares are classified as equity and details of the Group's share capital is disclosed in note (e) of the Parent Company's financial statements. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds. The Group also maintains the following reserves:

- Translation reserve – The translation reserve comprises all foreign exchange differences arising from the translation of the financial statements of foreign businesses.
- Hedging reserve – The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments that are determined to be an effective hedge.
- Retained earnings reserve – The retained earnings reserve comprises total cumulative recognised income and expense attributable to shareholders. Bonus issues of share capital and dividends to shareholders are also charged directly to this reserve. In addition the cost of acquiring shares in the Company and the liability to provide those shares to employees, is accounted for in this reserve.

Where any Group company purchases the Company's equity share capital and holds that share either directly as treasury shares or indirectly within an ESOP trust, the consideration paid, including any directly attributable incremental costs (net of income taxes), is deducted from equity attributable to the Company's equity holders until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders. These shares are used to satisfy share awards granted to Directors under the Group's share schemes. The Trustee purchases the Company's shares on the open market using loans made by the Company or a subsidiary of the Company.

1.19 Related parties

There are no related party transactions (other than with the key management) that are required to be disclosed in accordance with IAS24. Details of their remuneration are given in note 5 to the consolidated financial statements.

1.20 Accounting standards, interpretations and amendments to published standards not yet effective

The IASB has published a number of new IFRSs ("standards"), amendments and interpretations to existing standards which are not yet effective, but will be mandatory for the Group's accounting periods beginning on or after 1 October 2019. An assessment of the impact of these new standards and interpretations is set out below:

IFRS16 (Leases)

IFRS16 provides a comprehensive model for the identification of lease arrangements and their treatment in the financial statements for both lessors and lessees. IFRS16 supersedes the current lease guidance including IAS17 (*Leases*) for accounting periods beginning on or after 1 January 2019. The date of the initial application of IFRS16 for the Group is 1 October 2019.

IFRS16 requires the recognition of an asset and a corresponding liability for all leases with terms over 12 months unless the underlying asset is of a low value. The liability is measured at the present value of future lease payments for the lease term; depreciation of the assets and interest on the corresponding lease liabilities is recognised in the Income Statement over the lease term. In the cash flow statement, the total amount of cash paid is separated into the principal portion (within financing activities) and an interest portion (within operating activities).

The Group will adopt the modified retrospective approach and as such will not restate the prior year financial statements. On implementation of IFRS16 there will be a material increase in lease liabilities, along with a corresponding increase in right of use assets within property, plant and equipment. The Group's most significant leases relate to property.

Group Accounting Policies continued

For the year ended 30 September 2019

The estimated impact at the date of transition and the impact on the financial results in FY2020 is detailed below:

Financial statement line item		Impact
Property, plant and equipment	Increase	£34.0m
Net debt	Increase	£34.0m
Operating leases charge ¹ (currently)	Decrease	£7.0m
Depreciation	Increase	£6.4m
Interest	Increase	£1.3m
Adjusted PBT	Decrease	£0.7m

1 Applicable to those leases which fall under IFRS16.

The Group's activities as a lessor are not material and hence the Group does not expect any significant impact on the financial statements. However, some additional disclosures will be required from next year.

Other standards not yet effective

IFRIC23 (Uncertainty over Income Tax Treatments) is applicable for the year ending 30 September 2020 and clarifies how to apply the recognition and measurement requirements in IAS12 when there is uncertainty over the income tax treatments. The Group does not anticipate that the adoption of this standard will have a material impact on the Group.

1.21 Accounting estimates and judgements

The preparation of the Group's consolidated financial statements does not require management to make any critical accounting judgements, assumptions or estimates with regard to assets or liabilities that could potentially have a material adjustment to the carrying amount of assets or liabilities in the next 12 months.

Management however are required to make judgements, assumptions and estimates relating to certain assets and liabilities that could potentially have a material impact over the longer term. These relate to:

1.21.1 Acquisition accounting

When the Group makes an acquisition it recognises the identifiable assets and liabilities, including intangible assets, at fair value with the difference between the fair value of net assets acquired and the fair value of consideration paid comprising goodwill. Acquisitions are accounted for using the acquisition method as described in note 1.3 and 1.10 of the Group Accounting Policies. The key assumptions and estimates used to determine the valuation of intangible assets acquired are the forecast cash flows, the discount rate and customer/supplier attrition. Customer and supplier relationships are valued using an excess earnings cash flow model. Acquisitions often comprise an element of deferred consideration and may include a minority interest, which are subject to put options. These put options are valued at fair value at the date of acquisition. Deferred consideration is fair valued based on the Directors' estimate of future performance of the acquired entity.

The Group's growth strategy is underpinned by the successful execution of acquisitions. This results in material amounts of goodwill and intangible assets (principally customer and supplier relationships) being recognised in the Consolidated Statement of Financial Position. As set out in note 1.11 of the Group Accounting Policies, goodwill is tested annually to determine if there is any indication of impairment. Assumptions are then used to determine the recoverable amount of each CGU, principally based on the present value of estimated future cash flows to derive the "value in use" to the Group of the capitalised goodwill. The key estimates made and assumptions used in performing impairment testing this year are set out in note 10 to the consolidated financial statements.

1.21.2 Inventory provisions

Inventories are stated at the lower of cost and net realisable value as set out in note 1.12 of the Group Accounting Policies. In the course of normal trading activities, estimates are used to establish the net realisable value of inventory and impairment charges are made for obsolete or slow-moving inventories and against excess inventories.

The decision to make an impairment charge is based on a number of factors including management's assessment of the current trading environment, aged profiles and historical usage and other matters which are relevant at the time the consolidated financial statements are approved.

1.21.3 Defined benefit pension

Defined benefit pensions are accounted for as set out in note 1.6 of the Group Accounting Policies. Determining the value of the future defined benefit obligation requires estimates in respect of the assumptions used to calculate present values. These include discount rate, future mortality and inflation rate. Management makes these estimates in consultation with an independent actuary. Details of the estimates and key sensitivities made in calculating the defined benefit obligation at 30 September 2019 are set out in note 25 to the consolidated financial statements.

Parent Company Statement of Financial Position

As at 30 September 2019

	Note	2019 £m	2018 £m
Fixed assets			
Investments	d	78.8	72.0
Creditors: amounts falling due within one year			
Amounts owed to subsidiary undertakings		(27.6)	(14.4)
Total assets less current liabilities and net asset		51.2	57.6
Capital and reserves			
Called up share capital	e	5.7	5.7
Profit and loss account ¹		45.5	51.9
Total shareholders' equity		51.2	57.6

¹ Includes profit after tax for the year of £22.2m (2018: £30.9m).

The financial statements of Diploma PLC, company number 3899848, were approved by the Board of Directors on 18 November 2019 and signed on its behalf by:

JD Thomson
Chief Executive Officer

NP Lingwood
Group Finance Director

Parent Company Statement of Changes in Equity

For the year ended 30 September 2019

	Note	Share capital £m	Retained earnings £m	Total shareholders' equity £m
At 1 October 2017		5.7	49.2	54.9
Total Comprehensive Income	a	–	30.9	30.9
Dividends paid		–	(26.8)	(26.8)
Settlement of LTIP awards	e	–	(1.4)	(1.4)
At 30 September 2018		5.7	51.9	57.6
Total Comprehensive Income	a	–	22.2	22.2
Dividends paid		–	(29.8)	(29.8)
Settlement of LTIP awards	e	–	1.2	1.2
At 30 September 2019		5.7	45.5	51.2

Notes to the Parent Company Financial Statements

For the year ended 30 September 2019

a) Accounting policies

a.1) Basis of accounting

The Parent Company financial statements ("Financial Statements") have been prepared in accordance with the Companies Act 2006 and FRS101 (*Reduced Disclosures Framework*). The Directors confirm they have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future and accordingly, they continue to adopt the going concern basis in preparing the Financial Statements. The Financial Statements, which are prepared on a historical cost basis, are presented in UK sterling and all values are rounded to the nearest million pounds (£m) except when otherwise indicated.

The following disclosures have not been provided as permitted by FRS101:

- a cash flow statement and related notes;
- a comparative period reconciliation for share capital;
- disclosures in respect of transactions with wholly owned subsidiaries;
- disclosures in respect of capital management;
- the effects of new but not yet effective IFRS;
- disclosures in respect of the compensation of key management personnel as required.

The Company has also taken the exemption under FRS101 available in respect of the requirements of paragraphs 45(b) and 46 to 52 of IFRS2 (*Share-based Payment*) in respect of Group settled share-based payments as the consolidated financial statements of the Company include the equivalent disclosures within the Remuneration Committee Report.

a.2) Total Comprehensive Income

Total Comprehensive Income comprises dividends received from subsidiaries, interest payable on inter-company balances at the UK Base Rate, plus 1.5% and that are repayable on demand. Total Comprehensive Income is distributable to shareholders.

a.3) Dividends

Dividend income is recognised when received. Final dividend distributions are recognised in the Company's Financial Statements in the year in which the dividends are approved by the Company's shareholders. Interim dividends are recognised when paid.

The capacity of the Company to make dividend payments is primarily determined by the availability of retained distributable reserves and cash resources. As at 30 September 2019, the Company had distributable reserves of £45.5m (2018: £51.9m) and the total external dividends declared in 2019 amounted to £29.8m. When required the Company can receive dividends from its subsidiaries to further increase distributable reserves.

a.4) Diploma PLC Employment Benefit Trust and employee share schemes

Shares held by the Diploma PLC Employee Benefit Trust ("the Trust") are stated at cost and accounted for as a deduction from shareholders' equity in accordance with IAS32, as applied by FRS101. Shares that are held by the Trust are not eligible for dividends until such time as the awards have vested and options have been exercised by the participants.

a.5) Auditor's remuneration

Fees payable to the auditor for the audit of the Company's financial statements of £3,500 (2018: £3,500) were borne by a fellow Group undertaking.

b) Directors' and employees' remuneration

No remuneration is paid directly by the Company; information on the Directors' remuneration (which is paid by a subsidiary company) and their interests in the share capital of the Company are set out in the Remuneration Committee Report on pages 46 to 59. The Company had no employees (2018: none).

c) Company profit and loss account

As permitted by section 408 of the Companies Act 2006, no separate profit and loss account is presented for the Company. There were no gains or losses either in the current or preceding years recognised in Other Comprehensive Income. The Company's profit for the year was £22.2m (2018: profit of £30.9m), before settlement of LTIP awards.

d) Investments

	2019 £m	2018 £m
Shares in Group undertakings held at cost		
At 30 September	78.8	72.0

A full list of subsidiary and other related undertakings is set out on page 97.

e) Called up share capital

	2019 Number	2018 Number	2019 £m	2018 £m
Allotted, issued and fully paid ordinary shares of 5p each				
At 30 September	113,239,555	113,239,555	5.7	5.7

During the year 148,501 ordinary shares in the Company (2018: 92,530) were transferred from the Trust to participants on an after income tax basis in connection with the exercise of options in respect of awards which had vested under the 2011 Long Term Incentive Plan, as set out on pages 56 and 59 in the Remuneration Committee Report. The Trust also purchased 100,000 ordinary shares in the Company for £1.2m (2018: £1.2m) during the year. At 30 September 2019, the Trust held 51,867 (2018: 100,368) ordinary shares in the Company representing 0.1% of the called up share capital. The market value of the shares at 30 September 2019 was £0.9m (2018: £1.4m).

Independent auditors' report to the members of Diploma PLC

Report on the audit of the financial statements

Opinion

In our opinion:

- Diploma PLC's group financial statements and parent company financial statements (the "financial statements") give a true and fair view of the state of the group's and of the parent company's affairs as at 30 September 2019 and of the group's profit and cash flows for the year then ended;
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union;
- the parent company financial statements have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards, comprising FRS 101 "Reduced Disclosure Framework", and applicable law); and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements, included within the Annual Report & Accounts (the "Annual Report"), which comprise: the Consolidated and Parent Company Statements of Financial Position as at 30 September 2019; the Consolidated Income Statement and Consolidated Statement of Comprehensive Income, the Consolidated Cash Flow Statement, and the Consolidated and Parent Statement of Changes in Equity for the year then ended; the Group Accounting Policies; and the Notes to the Consolidated and Parent Company Financial Statements.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

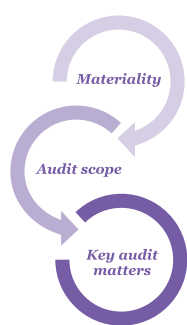
We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the FRC's Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

Other than those disclosed in note 27 to the financial statements, we have provided no non-audit services to the group or the parent company in the period from 1 October 2018 to 30 September 2019.

Our audit approach

Overview



- Overall group materiality: £4.2 million (2018: £3.6 million), based on 5% of profit before tax.
- Overall parent company materiality: £0.8 million (2018: £0.7 million), based on 1% of total assets.
- We conducted audit work over 22 reporting components across eight countries in which the group has significant operations.
- The reporting components where we performed an audit of their complete financial information accounted for 78% of group revenue and 82% of group profit before tax.
- The group engagement team performed the audit work on six of the reporting components, the audit of the parent company and visited, in person, two component teams which were responsible for the audit of seven reporting components across two countries. This included attendance at their audit clearance meetings and discussions on the audit approach and findings with those local teams.
- For those countries not visited in person we attended their clearance meetings via conference call or video conference.
- We maintained regular contact with local teams and evaluated the outcome of their work.
- Provision for impairment of inventories (group).
- Accounting for acquisitions (group).

Independent Auditors' Report to the Members of Diploma PLC continued

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

Capability of the audit in detecting irregularities, including fraud

Based on our understanding of the group and industry, we identified that the principal risks of non-compliance with laws and regulations related to tax and anti-bribery, and we considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries to improve the group's performance, and management bias in accounting estimates. The group engagement team shared this risk assessment with the component auditors so that they could include appropriate audit procedures in response to such risks in their work. Audit procedures performed by the group engagement team and/or component auditors included review of the financial statement disclosures to underlying supporting documentation, review of correspondence with the Financial Reporting Council, review of correspondence with legal advisors, enquiries of management, review of significant component auditors' work, review of internal audit reports in so far as they related to the financial statements and identifying and testing journal entries, including those posted with unusual account combinations.

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit.

Key audit matter	How our audit addressed the key audit matter
<p>Provision for impairment of inventories (group) Refer to page 88 (Accounting estimates and judgements) and note 15 (Inventories).</p> <p>The group holds significant levels of inventory with total inventory, at 30 September 2019, of £102.6m which is recorded net of a provision of £9.3m.</p> <p>There is a risk associated with the valuation of the inventory provision for slow moving and/or obsolete stock within each of the trading businesses. Determining the quantum of these provisions requires management estimation based on the level of stock, its ageing profile and its future demand.</p> <p>There is a risk that management are using the inventory provision to create variability in the Income Statement, resulting in a manipulation of the results in the financial year.</p>	<p>Our audit procedures included understanding and evaluating the controls and systems related to the inventory provision process, together with substantive audit procedures.</p> <p>The substantive audit procedures performed for each individual component varied depending on the nature of the trading business and the inventory provision methodology. The audit procedures included the following:</p> <ul style="list-style-type: none"> • We obtained management's inventory provision and checked the mathematical accuracy of the provision based upon the provision methodology in place for that component. • We tested, where applicable and on a sample basis, the accuracy of the ageing and demand reports used. • Our evaluation of the appropriateness of each of the trading businesses inventory provision methodology included checking that the methodology was consistent with the prior year or that changes were appropriate, assessing the appropriateness of key assumptions and considering the historic accuracy of provisions compared to write-offs. • We evaluated the appropriateness of the year on year movement in the provision and any significant charges or releases to the Income Statement. • We compared the actual sales value of a sample of inventory items to their book value to check that the carrying value of inventory did not exceed its net realisable value. <p>Based on the procedures, we did not identify any issues with the valuation of inventory or any instances of management using the inventory provision to create variability in the Income Statement.</p>

Key audit matter

How our audit addressed the key audit matter

Accounting for acquisitions (group)

Refer to page 88 (Accounting estimates and judgements) and note 22 (Acquisition of businesses).

The group completed four acquisitions during the year with the largest being the acquisition of Virginia Sealing Products (VSP) on 9 July 2019 for consideration of £57.2m.

Our audit focused on the valuation and allocation of the acquired intangibles, in particular managements' model for the allocation of the goodwill and intangibles of VSP, which requires significant management estimates. Management has recorded £40.0m of intangibles related to existing customer relationships and £14.7m of goodwill in respect of the VSP acquisition.

We engaged our internal valuations experts to assist with our audit procedures on the valuation and allocation of acquired intangibles and goodwill. We obtained management's valuation model and performed, amongst others, the following procedures:

- Tested the underlying mathematical accuracy of the model.
- Compared the cash flow forecasts used within the model to the Board approved budgets.
- Assessed the appropriateness of the key assumptions within the model, challenging management as appropriate. Specifically we:
 - Understood the revenue growth rates and profit margins in the forecast and assessed their appropriateness by comparing them to historical results.
 - Agreed key inputs to the discount rate to externally derived data and benchmarked against comparable companies.
 - Benchmarked the useful economic life attributed to customer relationships with comparable transactions in the market.
 - Corroborated the annual customer attrition rate to historic financial data.

Based on the procedures we performed we did not identify any material misstatements associated with the acquisition accounting.

We determined that there were no key audit matters applicable to the parent company to communicate in our report.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the group and the parent company, the accounting processes and controls, and the industry in which they operate.

The group is focused on three core sectors, Life Sciences, Seals and Controls with operations primarily geographically located in Australia, Canada, the USA, the UK and Continental Europe. Within the aforementioned sectors are a number of businesses / management reporting entities which are consolidated by group management. The financial statements are a consolidation of multiple reporting components representing the operating businesses within these three core sectors.

Our audit scope was determined by considering the significance of each component's contribution to profit before tax and contribution to individual financial statement line items, with specific consideration to obtaining sufficient coverage over significant risks and other areas of higher risk.

We identified 22 financial reporting components across eight countries for which we determined that full scope audits would need to be performed. This collectively gave us coverage of 78% of the group's revenue and 82% of the group's profit before tax. This, together with the additional procedures performed at the group level, gave us the evidence we needed for our opinion on the financial statements as a whole. The reporting components, excluding those audited by the group engagement team, were audited by eight component teams. The group engagement team visited two of the eight component teams, who were responsible for the audit of seven reporting components. The group engagement team met with local management, attended audit clearance meetings and discussed the audit approach and audit findings with the component teams. For those components not visited, the group engagement team attended their clearance meetings either via conference call or video conference.

Our attendance at the clearance meetings, review of discussion of the audit results at overseas locations, together with the additional procedures performed at group level, gave us the evidence we needed for our opinion on the financial statements as a whole. Our audit procedures at the group level included the audit of the consolidation, goodwill impairment review, pensions, and certain tax procedures. The group engagement team also performed the audit of the parent company.

Independent Auditors' Report to the Members of Diploma PLC continued

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

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

	Group financial statements	Parent Company financial statements
Overall materiality	£4.2 million (2018: £3.6 million).	£0.8 million (2018: £0.7 million).
How we determined it	5% of profit before tax.	1% of total assets.
Rationale for benchmark applied	We consider profit before tax to be an appropriate measure for a listed group and one of the key measures used by the shareholders in assessing the performance of the group.	We believe that total assets is the primary measure used by the shareholders in assessing the performance of a holding company and is a generally accepted auditing benchmark.

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. The range of materiality allocated across components was between £0.2 million and £3.8 million.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £210,000 (group audit) (2018: £184,000) and £38,000 (Parent company audit) (2018: £36,000) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Going concern

In accordance with ISAs (UK) we report as follows:

Reporting obligation	Outcome
We are required to report if we have anything material to add or draw attention to in respect of the directors' statement in the financial statements about whether the directors considered it appropriate to adopt the going concern basis of accounting in preparing the financial statements and the directors' identification of any material uncertainties to the group's and the parent company's ability to continue as a going concern over a period of at least twelve months from the date of approval of the financial statements.	We have nothing material to add or to draw attention to. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's and parent company's ability to continue as a going concern. For example, the terms on which the United Kingdom may withdraw from the European Union are not clear, and it is difficult to evaluate all of the potential implications on the group's trade, customers, suppliers and the wider economy.
We are required to report if the directors' statement relating to Going Concern in accordance with Listing Rule 9.8.6R(3) is materially inconsistent with our knowledge obtained in the audit.	We have nothing to report.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Directors' Report, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, the Companies Act 2006 (CA06), ISAs (UK) and the Listing Rules of the Financial Conduct Authority (FCA) require us also to report certain opinions and matters as described below (required by ISAs (UK) unless otherwise stated).

Strategic Report and Directors' Report

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Directors' Report for the year ended 30 September 2019 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Directors' Report. (CA06)

Corporate Governance Statement

In our opinion, based on the work undertaken in the course of the audit, the information given in the Corporate Governance Statement (on page 40) about internal controls and risk management systems in relation to financial reporting processes in compliance with rules 7.2.5 and 7.2.6 of the Disclosure Guidance and Transparency Rules sourcebook of the FCA ("DTR") is consistent with the financial statements and has been prepared in accordance with applicable legal requirements. (CA06)

In light of the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit, we did not identify any material misstatements in this information. (CA06)

In our opinion, based on the work undertaken in the course of the audit, the information given in the Corporate Governance Statement (on pages 36 to 40) with respect to the parent company's corporate governance code and practices and about its administrative, management and supervisory bodies and their committees complies with rules 7.2.2, 7.2.3 and 7.2.7 of the DTR. (CA06)

We have nothing to report arising from our responsibility to report if a corporate governance statement has not been prepared by the parent company. (CA06)

The directors' assessment of the prospects of the group and of the principal risks that would threaten the solvency or liquidity of the group

We have nothing material to add or draw attention to regarding:

- The directors' confirmation on page 28 of the Annual Report that they have carried out a robust assessment of the principal risks facing the group, including those that would threaten its business model, future performance, solvency or liquidity.
- The disclosures in the Annual Report that describe those risks and explain how they are being managed or mitigated.
- The directors' explanation on page 28 of the Annual Report as to how they have assessed the prospects of the group, over what period they have done so and why they consider that period to be appropriate, and their statement as to whether they have a reasonable expectation that the group will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, including any related disclosures drawing attention to any necessary qualifications or assumptions.

We have nothing to report having performed a review of the directors' statement that they have carried out a robust assessment of the principal risks facing the group and statement in relation to the longer-term viability of the group. Our review was substantially less in scope than an audit and only consisted of making inquiries and considering the directors' process supporting their statements; checking that the statements are in alignment with the relevant provisions of the UK Corporate Governance Code (the "Code"); and considering whether the statements are consistent with the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit. (Listing Rules)

Other Code Provisions

We have nothing to report in respect of our responsibility to report when:

- The statement given by the directors, on page 61, that they consider the Annual Report taken as a whole to be fair, balanced and understandable, and provides the information necessary for the members to assess the group's and parent company's position and performance, business model and strategy is materially inconsistent with our knowledge of the group and parent company obtained in the course of performing our audit.
- The section of the Annual Report on page 42 describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.
- The directors' statement relating to the parent company's compliance with the Code does not properly disclose a departure from a relevant provision of the Code specified, under the Listing Rules, for review by the auditors.

Directors' Remuneration

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006. (CA06)

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of Directors' responsibilities for preparing the financial statements set out on page 61, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Independent Auditors' Report to the Members of Diploma PLC continued

Auditors' responsibilities for the audit of the financial statements

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

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

Use of this report

This report, including the opinions, has been prepared for and only for the parent company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the Audit Committee, we were appointed by the members on 1 March 2018 to audit the financial statements for the year ended 30 September 2018 and subsequent financial periods. The period of total uninterrupted engagement is 2 years, covering the years ended 30 September 2018 and 30 September 2019.

Christopher Burns (Senior Statutory Auditor) for and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors
London
18 November 2019

Subsidiaries of Diploma PLC

	Registered Office address*	Registered Office address*	
Life Sciences			
Somagen Diagnostics Inc.	F	Cablecraft Limited	
AMT Electrosurgery Inc.	V	Birch Valley Plastics Limited ¹	
Vantage Endoscopy Inc.	V	Krempfast Limited ²	
Big Green Surgical Company Pty Limited	X	Betaduct Limited ¹	
Diagnostic Solutions Pty Limited	X	Hawco Limited	
Sphere Surgical Pty Limited	X	Abbeychart Limited ¹	
Aspire Surgical Pty Limited	X	HA Wainwright Limited ¹	
Diploma Healthcare Group NZ Limited	Z	Hawco Refrigeration Limited ¹	
Techno-Path (Distribution) Limited	AC	Hawco, Inc.	
Abacus dx Pty Limited	X	Microtherm UK Limited ¹	
Abacus dx Limited	Z	IS Group (Europe) Limited ¹	
A1-CBISS Limited	A	Specialty Fasteners Limited ¹	
a1-envirosciences GmbH	G	Specialty Fasteners & Components Limited ¹	
a1-Envirosciences Limited ¹	A	FSC UK Limited ¹	
Hitek Limited ¹	A	FS Cables limited	
Hitek Group Limited ¹	A	FSC Global Limited ²	
		Caplink Limited ¹	
Seals			
HB Sealing Products Inc.	D	Intermediate holding companies	
HKX Inc.	E	Diploma Holdings PLC	A
RTD Seals Corp.	C	Diploma Holdings Inc.	C
VSP Technologies, Inc.	C	Pride Limited	A
HB Sealing Products Limited	W	Diploma Australia Holdings Limited	A
M Seals A/S ³	S	Diploma Canada Holdings Limited	A
M Seals AB ³	T	Diploma Overseas Limited	A
M Seals UK Limited ²	A	Napier Group Limited	A
EDCO Seal and Supply Limited ²	A	Williamson, Cliff Limited	A
Diploma (Tianjin) Trading Co. Limited	AB	Newlandglebe Limited	A
FPE Seals Limited	A	Diploma Holding Germany GmbH	H
DMR Seals (Holdings) Limited ²	A	Diploma Canada Healthcare Inc.	F
DMR Gaskets Limited ²	A	Diploma Australia Healthcare Pty Limited	X
DMR Seals Limited ²	A	Diploma Australia Seals Pty Limited	X
A.B. Seals Limited ¹	A		
Swan Seals (Aberdeen) Limited ¹	A		
FPE Seals BV	P		
Kentek Oy ³	K		
ZAO Kentek ³	O		
Kentek Eesti Ou ³	L		
SIA Kentek Latvija ³	M		
UAB Kentek Lietuva ³	N		
Kubo Tech AG	Q		
Kubo Form AG	Q		
Kubo Tech GmbH	R		
TotalSeal Group Australia Pty Limited	Y		
West Coast Industrial Supplies New Caledonia SAS	AA		
Controls			
IS-Rayfast Limited	A		
IS-Motorsport, Inc.	C		
Amfast Limited ¹	A		
Clarendon Specialty Fasteners Limited	A		
Clarendon Specialty Fasteners, Inc.	B		
Clarendon Engineering Supplies Limited ¹	A		
Cabletec Interconnect Component Systems Limited ¹	A		
Sommer GmbH	H		
Filcon Electronic GmbH	I		
Actios SAS	U		
Deem Electronic & Electric Material Co. Limited ⁴	AD		
Gremtek SAS	U		
Gremco UK Limited ²	A		
Gremtek GmbH	J		
Ascome SARL	U		

- 1 Dormant company.
- 2 These subsidiaries, which are incorporated in England, are exempt from the requirements of the UK Companies Act 2006 relating to the audit of individual accounts by virtue of section 479A of the Act.
- 3 These subsidiaries are 90% owned, all other subsidiaries are wholly owned, with the exception of Deem Electronic & Electric Material Co Ltd (see note 4 below).
- 4 This subsidiary is 70% owned.

All subsidiaries are owned through ordinary shares.

* Registered Office address

- A 12 Charterhouse Square, London, EC1M 6AX, UK.
- B 5716 Corsa Avenue, Ste 110, Westlake Village, CA 91362-7354, USA.
- C 919 North Market Street, Suite 950, Wilmington, DE 19801, USA.
- D 17888 67th Court North, Loxahatchee, FL 33470-2525, USA.
- E 4505 Pacific Highway East, Suite C2, Fife, WA 98424-2638, USA.
- F 3400 First Canadian Centre, 350-7th Avenue SW, Calgary, Alberta T2P 3N9, Canada.
- G Eichsfelder Strasse 1, 40595, Düsseldorf, Germany.
- H Kraichgaustrasse 5, D-73765 Neuhausen, Germany.
- I Rotwandweg 5, D-82024, Taufkirchen/München, Germany.
- J 20-24 Robert Bosch Strasse, 25451 Quickborn, Germany.
- K Nuolikuja 8, FI-01740, Vantaa, Finland.
- L Laki tn 16, Kristiine linnaosa, Tallinn, Harju maakond, 10621, Estonia.
- M Maskavas iela 459, Riga, LV-1063, Latvija.
- N Vilniaus r. sav., Bukiškių k., Bičiulių g. 29, Lithuania.
- O Dom 2, Liter B, Proezd Mebel'nyj, 197374, St. Petersburg, Russia.
- P Industrieterrein Dombosch 1, Eftweg 38, 4941 VP Raamsdonksveer, the Netherlands.
- Q Im Langhag 5, 8307 Illnau-Effretikon, Switzerland.
- R Gewerbeallee 12a, 4221 Steyregg, Austria.
- S Bybjergvej 13, DK 3060, Espergaerde, Denmark.
- T Industrivägen 17, SE-302, 41 Halmstad, Sweden.
- U 58 rue du Fosse blanc, 92230 Gennevilliers, France.
- V 333 Bay St., Suite 2400, Toronto, Ontario M5H 2T6, Canada.
- W 226 Lockhart Road, Barrie, Ontario, L4N 9G8, Canada.
- X 46 Albert Street, Preston, Victoria, 3072, Australia.
- Y 72 Platinum Street, Crestmead, Queensland, 4132, Australia.
- Z Office of Bendall & Cant Ltd, Southern Cross Building, 61 High Street, Auckland, New Zealand.
- AA 22 Avenue des Géomètres Pionniers, ZAC PANDA – 98835, Dumbéa, New Caledonia.
- AB 18 Fuyuangdao Road, Wuqing Development Area, Tianjin, China.
- AC Fort Henry Business Park, Ballina, Co. Tipperary, Ireland.
- AD N°25-15A Yao Bei Road, Yao Jia Industrial Zone, Ganjingzi District, Dalian, China.

Financial Calendar and Shareholder Information

Announcements (provisional dates)

First Quarter Statement released	15 January 2020
Annual General Meeting (2019)	15 January 2020
Second Quarter Statement released	25 March 2020
Half Year Results announced	11 May 2020
Third Quarter Statement released	27 August 2020
Preliminary Results announced	16 November 2020
Annual Report posted to shareholders	4 December 2020
Annual General Meeting (2020)	20 January 2021

Dividends (provisional dates)

Interim announced	11 May 2020
Paid	10 June 2020
Final announced	16 November 2020
Paid (if approved)	27 January 2021

Annual Report & Accounts

Copies can be obtained from the Group Company Secretary at the address shown across.

Share Registrar – Computershare Investor Services PLC

The Company's Registrar is:
Computershare Investor Services PLC
The Pavilions
Bridgwater Road
Bristol BS99 6ZZ
Telephone: 0370 7020010

Its website for shareholder enquiries is:
www.computershare.co.uk

Shareholders' enquiries

If you have any enquiry about the Company's business or about something affecting you as a shareholder (other than questions dealt with by Computershare Investor Services PLC) you are invited to contact the Group Company Secretary at the address shown below.

Group Company Secretary and Registered Office

AJ Gallagher FCIS
Solicitor
12 Charterhouse Square
London EC1M 6AX
Telephone: 020 7549 5700

Registered in England and Wales, number 3899848.

Website

Diploma's website is www.diplomaplc.com

Advisors

Investment Bankers

Lazard
50 Stratton Street
London W1J 8LL

Corporate Stockbrokers

Numis Securities
10 Paternoster Square
London EC4M 7LT

Barclays Bank PLC

1 Churchill Place
London E14 5HP

Independent Auditor

PricewaterhouseCoopers LLP
1 Embankment Place
London WC2N 6RH

Solicitors

Simmons & Simmons LLP
CityPoint
One Ropemaker Street
London EC2Y 9SS

Bankers

Barclays Bank PLC
1 Churchill Place
London E14 5HP

HSBC Bank plc

City Corporate Banking Centre
60 Queen Victoria Street
London EC4N 4TR

Five Year Record

Year ended 30 September	2019 £m	2018 £m	2017 £m	2016 £m	2015 £m
Revenue	544.7	485.1	451.9	382.6	333.8
Adjusted operating profit	97.2	84.9	78.2	65.7	60.3
Finance expense, net	(0.7)	(0.1)	(0.7)	(0.8)	(0.7)
Adjusted profit before tax	96.5	84.8	77.5	64.9	59.6
Acquisition related charges	(13.1)	(9.6)	(9.7)	(10.3)	(7.4)
(CEO transition costs)/gain on disposal of assets	–	(2.1)	–	0.7	–
Fair value remeasurements	0.1	(0.4)	(1.0)	(1.3)	(0.4)
Profit before tax	83.5	72.7	66.8	54.0	51.8
Tax expense	(21.1)	(18.3)	(18.6)	(14.9)	(14.4)
Profit for the year	62.4	54.4	48.2	39.1	37.4
Capital structure					
Equity shareholders' funds	321.3	291.2	262.0	233.5	189.6
Minority interest	3.3	3.1	4.8	4.3	5.2
Add/(deduct): cash and cash equivalents	(27.0)	(36.0)	(22.3)	(20.6)	(23.0)
borrowings	42.1	–	–	10.0	20.0
retirement benefit obligations	17.8	10.5	9.9	17.2	9.8
acquisition liabilities	11.3	5.6	6.6	6.8	6.6
deferred tax, net	8.3	8.4	8.2	7.4	5.9
Reported trading capital employed	377.1	282.8	269.2	258.6	214.1
Add: historic goodwill and acquisition related charges, net of deferred tax	84.3	74.6	66.3	59.2	53.6
Adjusted trading capital employed	461.4	357.4	335.5	317.8	267.7
Net (decrease)/increase in net (debt)/funds	(51.9)	13.1	11.9	4.9	(17.4)
Add: dividends paid	30.1	27.0	23.7	21.4	19.9
acquisition of businesses	78.3	20.4	20.1	32.7	37.8
Free cash flow⁷	56.5	60.5	55.7	59.0	40.3
Per ordinary share (pence)					
Basic earnings	54.7	47.5	42.0	33.9	32.5
Adjusted earnings	64.3	56.4	49.8	41.9	38.2
Free cash flow	49.9	53.5	49.3	52.2	35.6
Dividends	29.0	25.5	23.0	20.0	18.2
Total shareholders' equity	284	257	232	206	167
Dividend cover	2.2	2.2	2.2	2.1	2.1
Ratios	%	%	%	%	%
Return on adjusted trading capital employed ("ROATCE")	22.9	24.5	24.0	21.1	23.9
Working capital: revenue	16.5	15.1	15.0	16.6	17.0
Adjusted operating margin	17.8	17.5	17.3	17.2	18.1

1 Acquisition related charges comprise the amortisation and impairment of acquisition intangible assets, acquisitions expenses and adjustments to deferred consideration.

2 Acquisition liabilities comprise amounts payable for the future purchases of minority interests and deferred consideration.

3 ROATCE represents adjusted operating profit, before acquisition related charges (adjusted for the full year effect of acquisitions and disposals), as a percentage of adjusted trading capital employed. Trading capital employed and adjusted trading capital employed are calculated as defined in note 2 to the consolidated financial statements.

4 Adjusted earnings per share is calculated in accordance with note 9 to the consolidated financial statements.

5 Total shareholders' equity per share has been calculated by dividing equity shareholders' funds by the number of ordinary shares in issue at the year end.

6 Dividend cover is calculated on adjusted earnings as defined in note 2 to the consolidated financial statements.

7 Free cash flow is defined in note 2 to the consolidated financial statements. Free cash flow per share is the free cash flow balance divided by the number of ordinary shares in issue at the year end.

Notes

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