AIREA plc

Preliminary results for the year ended 30th June 2016

Strategic Report

Airea plc is pleased to be able to report that the business has made substantial progress in the year:

- Operating profit up 86% to £2.0m
- Basic earnings per share up 133% to 3.01p
- EBITDA[1] before exceptional items up 48% to £2.8m
- Proposed final dividend up 67% to 1.5p

Principal activity and strategy

The group remains focused on the manufacture, marketing and distribution of floor coverings. Our approach to strategy is uncomplicated; to develop products that sell, exploit the strength of our combined manufacturing and distribution operation, and deliver robust cash flows.

Overview

Airea plc is pleased to report an 86% increase in operating profit following an improvement in UK contract sales and operating margins and despite the adverse impact on international sales of the strength of sterling against the Euro during the period.

As reported in the interim announcement, the second half also benefited from a reduced cost base following the consolidation of operations onto two existing sites occupied by the business at Ossett and Wakefield. One of the properties came to the end of the lease period and has been vacated. The other freehold property remains in our ownership and has been leased to a third party. This brings to fruition a process whereby the property footprint has progressively reduced over the last four years, cutting the number of sites occupied from six to two. The move not only delivers considerable cost savings, but enhances our operational capability, reducing lead times and thereby improving customer service.

The exceptional one off costs incurred as a consequence of site reorganisation i.e. rationalisation of finished inventories, redundancy payments to staff who were not able to transfer, and the relocation of equipment and inventory have been highlighted in the income statement.

Despite the deterioration in the financial climate, we were able to reduce the pension deficit by completing a Pension Increase Exchange exercise. The initiative allowed pensioners to opt for an income stream more aligned to their personal circumstances and preferences, whilst at the same time reducing the cost of past service benefits to the scheme. The gain to profit is highlighted as exceptional in the income statement. In addition, the pension scheme investment strategy is constantly under review, and our liability hedging strategy and increased diversification have performed well.

As in previous years the cost base remains under constant review and operating margin increased in the year.

A further repurchase of shares was completed in the period, funded from cash flow generated in the year, and contributed to the improvement in earnings per share. Cash generation increased and the group continues to operate debt free.

Group results

Revenue for the period was £24.6m (2015 £25.5m) as the strength of sterling against the Euro had an adverse impact on our sales into continental Europe, especially in the first half of the financial year the GBP/Euro exchange rate at 1.40-1.44 for long periods had a detrimental effect on sales in highly competitive, price sensitive markets. Operating profit before exceptional items was £2,013,000 (2015: £1,212,000), due to improved operating margin, and the lower cost base, largely resulting from the site consolidation in the second half. The exceptional charge of £1.3m relates to the costs associated with the consolidation of manufacturing operations, and the exceptional income of £1.3m related to the Pension Increase Exchange. The operating profit after exceptional items was £2,042,000 (2015: £1,098,000). Other finance costs relating to the defined benefit pension scheme increased to £651,000 (2015: £447,000) as a result of changes in the Pension Protection Fund Levy. After charging tax of £114,000 (2015 £69,000), the profit for the year was £1,277,000 (2015: £581,000).

Basic earnings per share were 3.01p (2015: 1.29p), and basic adjusted earnings per share[2] were 2.96p (2015: 1.50p).

Operating cash flows before exceptional items, movements in working capital and other payables were £2,844,000 (2015: £1,928,000). After taking account of exceptional items of £803,000 (2015: nil) operating cash flows before movements in working capital and other payables were £2,041,000 (2015: £1,928,000). Working capital decreased by £1,009,000 (2015: increase £490,000) due to a reduction in inventories. Contributions of £400,000 (2015: £400,000) were made to the defined benefit pension scheme in line with the agreement reached with the trustees based on the 2014 actuarial valuation. Capital expenditure of £704,000 (2015: £459,000) remained focussed on supporting new product launches and the ongoing improvement in the flexibility, reliability and productivity of the manufacturing process. A repurchase of 2,050,000 ordinary shares was completed at a cost of £410,000.

The reduction of the pension deficit to £6.7m (2015 £7.4m) stemmed from the net effect of the Pension Increase Exchange exercise, the deterioration in corporate bond yields and the bigger Pension Protection Fund Levy, which diverts company contributions from funding the pension plan.

Key performance indicators

As part of its internal financial control procedures the board monitors certain financial ratios. For the year to 30th June 2016 value added per employee (the ratio of sales less material costs to average employee numbers) amounted to £70,000 (2015: £70,000), operating return on sales (the ratio of operating profit before exceptional items to revenue) was 8.2% (2015: 4.7%), return on average net operating assets (the ratio of operating profit before exceptional items to average operating assets) was 11.0% (2015: 7.1%) and working capital to sales percentage was 34.3% (2015: 38.2%). The improvement in the ratios demonstrates the reduction in the cost base and the improvement in working capital efficiency.

Principal risks and uncertainties

The board has responsibility for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives, and ensuring that risks are managed effectively across the group. Risks are identified as being principally based on the likelihood of occurrence and potential impact on the group. The group's principal risks are identified below, together with a description of how the group mitigates those risks.

The key operational risk facing the business continues to be the competitive nature of the markets for the group's products. To mitigate this risk the group seeks to improve existing products, introduce new products and achieve high levels of customer service and efficiency.

The majority of the group's revenue arises from trade with flooring contractors and independent retailers. The activity levels within this customer base are determined by consumer demand created through a wide range of commercial refurbishment and building projects and activity in the housing market. The general level of activity in these underlying markets has the potential to affect the demand for products supplied by the group. The group mitigates these factors by closely monitoring sales trends and taking appropriate action early, along with strengthening the product range and developing new channels to market, both at home and abroad, to grow demand across a wider range of markets.

The group operates a defined benefit pension scheme. At present, in aggregate, there is an actuarial deficit between the value of the projected liabilities of this scheme and the assets they hold. The amount of the deficit may be adversely affected by changes in a number of factors, including investment returns, long-term interest rate and price inflation expectations, and anticipated members' longevity. Further increases in pension scheme deficit may require the group to increase the amount of cash contributions payable to the scheme, thereby reducing cash available to meet the group's other operating, investing and financing requirements. Following the triennial funding valuation of the group's pension scheme in 2014, a revised deficit recovery plan was agreed. The performance of the group's pension scheme and deficit recovery plan are regularly reviewed by both the group and the trustees of the scheme, taking actuarial and investment advice as appropriate. The results of these reviews are discussed with the board and appropriate action taken.

Other risks

Raw material costs are a significant constituent of overall product cost, and are impacted by global commodity markets. Significant fluctuations in raw material costs can have a material impact on profitability. The group continuously seeks out opportunities to develop a robust and competitive supply base, substitute new materials and closely monitors selling prices and margins.

The global nature of the group's business means it is exposed to volatility in currency exchange rates in respect of foreign currency denominated transactions, the most significant being the euro. In order to protect itself against currency fluctuations the group has taken advantage of the opportunity to naturally hedge euro revenue with euro payments. This is done in combination with foreign currency bank accounts and forward exchange contracts. No transactions of a speculative nature are undertaken.

Other risks include the availability of necessary materials, business interruption and the duty of care to our employees, customers and the wider public. These risks are managed through the combination of quality assurance and health and safety procedures, and insurance cover.

Management and personnel

The improvement in the financial performance of the business is testament to the flexibility, hard work and outstanding commitment of our staff, we once again thank everyone in the business for their contribution.

Current trading and future prospects

After a number of years of strengthening sterling, we are now enjoying a more competitive exchange rate, which offers potential opportunities to restore growth in our export business, and improve our competitive position against international competition in the home market. Marginal pricing is however common in many of the markets we serve and it is highly unlikely that our competition will change pricing habits completely despite the additional pressure from currency. Of most concern is the threat of depressed market activity within the construction sector generally which has the potential to overwhelm any price and cost advantages we may enjoy.

As ever our plans do not assume any help from the market and whilst the board notes the uncertainty arising from the political and economic changes currently taking place, our focus is on exploiting the expanding opportunities that arise from the repositioning of the business over recent years.

The site consolidation is now almost complete although we are reviewing our position concerning one of our remaining lease properties, and is delivering cost savings and operational improvements significantly ahead of expectations.

New strategic investment in manufacturing technology provides the spring board for extending the product range to new market sectors, and this combined with a lower cost base gives us real cause for optimism for dealing with growing economic uncertainty.

We believe the Group is well positioned for growth .

Given our confidence in the future prospects of the business, the ongoing improvement in the performance of the business, and a robust cash flow, we are once again able to support the progressive dividend policy. If approved, a final dividend of 1.5p per share will be paid on 24th November 2016 to shareholders on the register at close of business on 28th October 2016. The ex dividend date is 27th October 2016.

[1] EBITDA, is earnings before depreciation, interest, taxation and amortisation

[2] Adjusted earnings are earnings adjusted for exceptional operating items (net of tax)

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This announcement contains inside information for the purposes of Article 7 of EU Regulation 596/2014.

The financial information set out in the announcement does not constitute the group's statutory accounts for the years ended 30 June 2016 or 30 June 2015. The financial information for the year ended 30 June 2015 is derived from the statutory accounts for that year which have been delivered to the Registrar of Companies. The auditors reported on those accounts; their report was unqualified and did not include any statement under s498(2) or s498(3) of the Companies Act 2006. The consolidated balance sheet at 30 June 2016, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated cash flow statement and the consolidated statement of changes in equity for the year then ended have been extracted from the Group's 2016 statutory financial statements upon which the auditor's opinion is unqualified and does not include any statement under s498(2) or s498(3) of the Companies Act 2006.

The announcement has been agreed with the company's auditor for release.

Audited Consolidated Income Statement

Year ended 30th June 2016

	2016	2015
	£000	£000
Revenue	24,577	25,538
Operating costs	(22,535)	(24,440)
Operating profit before exceptional items	2,013	1,212
Exceptional costs	(1,271)	(114)
Pension credit	1,300	-
Operating profit	2,042	1,098
Finance income	-	1
Finance costs	(651)	(449)
Profit before taxation	1,391	650
Taxation	(114)	(69)
Profit attributable to the shareholders of the group	1,277	581
Earnings per share (basic and diluted)	3.01 p	1.29 p

All amounts relate to continuing operations

Audited Consolidated Statement of Comprehensive Income

Year ended 30th June 2016

	2016		2015	
	£000	£000	£000	£000
Profit attributable to shareholders of the group		1,277		581
Actuarial loss recognised in the pension scheme	(291)		(1,635)	
Related deferred taxation	(83)		267	
		(374)		(1,368)
Unrealised valuation gain	3,009		-	
Related deferred taxation	(240)		-	
		2,769		-
Total other comprehensive income		2,395		(1,368)
Total comprehensive income attributable to the shareholders of the group		3,672		(787)

All items will not be reclassified as profit and loss.

Audited Consolidated Balance Sheet

as at 30th June 2016

	2016		2015	
	£000	£000	£000	£000
Non-current assets				
Property, plant and equipment		5,489		5,333
Investment property		2,701		-
Deferred tax asset		1,264		1,557
		9,454		6,890
Current assets				
Inventories	9,338		10,647	
Trade and other receivables	4,601		4,412	
Cash and cash equivalents	3,114		1,883	
		17,053		16,942
Total assets		26,507		23,832
Current liabilities				
Trade and other payables	(5,505)		(5,308)	
Provisions	(125)		-	
		(5,630)		(5,308)
Non-current liabilities				
Pension deficit	(6,685)		(7,443)	
Deferred tax	(241)		(1)	
		(6,926)		(7,444)
Total liabilities		(12,556)		(12,752)
		13,951		11,080
Equity				
Called up share capital		10,339		10,851
Share premium account		504		504
Capital redemption reserve		3,617		3,105
Revaluation reserve		3,009		-
Retained earnings		(3,518)		(3,380)
		13,951		11,080

Audited Consolidated Cash Flow Statement

Year ended 30th June 2016

	2016	2015
	£000	£000
Cash flow from operating activities		
Profit for the year	1,277	581
Tax charged	114	69
Finance costs	651	448
Depreciation	837	830
Profit on disposal of property, plant and equipment	(6)	-
Pension credit	(1,300)	-
Inventory Impairment	468	-
Operating cash flows before movements in working capital	2,041	1,928
Decrease/(increase) in inventories	841	(427)
Increase in trade and other receivables	(189)	(99)
Increase in trade and other payables	232	151
Increase/(decrease) in provisions for liabilities and charges	125	(115)
Cash generated from operations	3,050	1,438
Income tax received	61	-
Contributions to defined benefit pension scheme	(400)	(400)
Net cash generated from operations	2,711	1,038
Investing activities		
Purchase of property, plant and equipment	(704)	(459)
Proceeds on disposal of property, plant and equipment	25	-
	(679)	(459)
Financing activities		
Interest	-	(1)
Share repurchase	(410)	(348)
Equity dividends paid	(391)	(277)
	(801)	(626)
Net increase/(decrease) in cash and cash equivalents	1,231	(47)
Cash and cash equivalents at start of the year	1,883	1,930
Cash and cash equivalents at end of the year	3,114	1,883

Audited Consolidated Statement of Changes in Equity

Year ended 30th June 2016

	Share capital	Share premium account	Capital redemption reserve	Revaluation Reserve	Profit and loss account	Total equity
	£000	£000	£000	£000	£000	£000
At 1st July 2014	11,561	504	2,395	-	(1,968)	12,492
Comprehensive income for then year						
Profit for the year	-	-	-	-	581	581
Other comprehensive income for the year	-	-	-	-	(1,368)	(1,368)
Total comprehensive income for the year	-	-	-	-	(787)	(787)
Contributions by and distributions to owners						
Share repurchase	(710)	-	710	-	-	-
Consideration paid on share purchase	-	-	-	-	(348)	(348)
Dividend paid	-	-	-	-	(277)	(277)
Total contributions by and distributions to owners	(710)	-	710	-	(625)	(625)
At 30th June and 1st July 2015	10,851	504	3,105	-	(3,380)	11,080
Comprehensive Income for the year						
Profit for the year	-	-	-	-	1,277	1,277
Other comprehensive income for the year	-	-	-	3,009	(614)	2,395
Total comprehensive income for the year	-	-	-	3,009	663	3,672
Contributions by and distributions to owners						
Share repurchase	(512)	-	512	-	-	-
Consideration paid on share purchase	-	-	-	-	(410)	(410)
Dividend paid	-	-	-	-	(391)	(391)
Total Contributions by and distributions to owners	(512)	-	512	-	(801)	(801)
At 30th June 2016	10,339	504	3,617	3,009	(3,518)	13,951

In accordance with Rule 20 of the AIM Rules, Airea confirms that the annual report and accounts for the year ended 30th June 2016 will be available to view on the Company's website at www.aireaplc.co.uk on 8th September 2016, and will be posted to shareholders by 16th September 2016.