Growth & Resilience - introduction

Stephen Harris, CEO
Today’s agenda...

1) Introductory presentation  
   Stephen Harris

2) Insight into growth opportunities  
   Divisional Management

3) Modeling growth – and a possible downturn  
   David Landless

4) Summary  
   Stephen Harris
Bodycote processes

THERMAL PROCESSING

Heat treatment
Highly precise improvement of properties in metal components

Hot Isostatic Pressing (HIP)
The ultimate strengthening process

Surface Technology
Temperature and wear protection

GLOBAL LEADERSHIP
Independent thermal processors

- Overall market estimated at £20bn*
- c20% outsourced to independents
- Bodycote the only global player
- Handful of regional players
- Mostly localised groups or single site operations

* Management estimate

Bodycote 3x bigger than next largest player
What is heat treatment?

- Precise temperature cycling in controlled atmosphere
- Changes crystal structure
- Creates ‘diffusion’ layer
- Changes internal stresses
- Improves properties, e.g.: Strength, Hardness, Wear resistance, Corrosion resistance

Different cycles and gases produce different characteristics.
What is HIP?

- **Hot:** up to 2,000°C
- **Isostatic:** omnidirectional inert gas pressure
- **Pressure:** up to 45,000 psi

- Eliminates porosity in castings or sintered components
- Improves density
- Improves material properties, e.g. strength
What is surface technology?

- A group of processes used to apply a ceramic or cermet coating to metals
- Includes plasma spray, HVOF and thermo-chemically formed ceramics
- Finely divided metallic or non-metallic materials, usually in powder form, are deposited onto the surface of components in a semi-molten state

Improves wear and temperature resistance
The value proposition

Heat treatment
An essential enabler of modern technology

- Optimises strength where it’s needed
- Process control – total predictability
- Mission critical

Bodycote
Scale benefits:
- 170 plants
- 1,920 process lines

- Multiple processes and multiple plants are major advantage to customers
- Network simplifies complexity
- Economies of scale:
  - Freight and energy
  - Equipment utilisation
Where is Bodycote?

170 plants · 27 countries · 1,920 process lines · 5,500 employees
Spread of activities 2011 H1 sales

Markets

General Industrial 42%
Aerospace 20%
Automotive 26%

Energy 12%

Growth & Resilience - introduction

Geography

North America 28%
France 17%
Emerging 10%
Nordic 12%
Germanic 13%
Low Countries 6%
Southern Europe 2%
Other 2%
Performance history excludes Testing, at 2011 exchange rates

Prior to 2008

- Network expansion
- Growth via acquisitions & greenfields
- Substantial investment

BUT

- Capital utilisation weak
- Cash generation weak
- Business ‘quality’ erosion
2009 – a new beginning
- Major restructuring
- Withdrawal from low profit, low potential plants
- Bench strength enhanced
- New focus

New focus
- Business ‘quality’
- Capital efficiency
- Higher-value opportunities
- Better margins
- Strong cash
- And good growth too

* Excludes Testing, at 2011 exchange rates
Our strategy

- Maximise return on existing assets
- Enhance business processes
- Divisional market focus
- Migrate with our customers to emerging markets
- Longer term growth from targeting proprietary technologies
Investing in five drivers for growth

- Aero & Energy Secular Growth
- Emerging Markets
- Technology Change
- HIP Product Fabrication
- S³P
Aerospace & Energy – Secular Growth Markets
Market characteristics:
- Advanced requirements
- Low volumes
- Complex supply chains
- Late cycle

Bodycote characteristics:
- Specialist state-of-the-art plants
- Nadcap quality accreditations
- Global
Bodycote’s processes

Aero and gas turbine components must operate in high temperatures. Heat treatment, HIP and surface coatings are essential.

- Cast blades are “HIPed” to increase their creep & fatigue resistance
- Honeycomb is vacuum brazed onto the vanes
- Precipitation hardened to increase strength at high temp.
- Thermal spray coating to improve temperature resistance

Multiple processes required – only Bodycote has them all
### Global market position

**Aerospace, defence and energy**

<table>
<thead>
<tr>
<th>ADE proportions</th>
<th>Plants</th>
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<tbody>
<tr>
<td><strong>Heat treatment</strong></td>
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<tr>
<td>c60%</td>
<td>37 ADE specialist</td>
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<th>Hot Isostatic Pressing (HIP)</th>
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<tr>
<td>c30%</td>
<td>10 specialist</td>
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<th>Surface technology</th>
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<td>c10%</td>
<td>5 specialist</td>
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**Leading global player - HT and HIP**
Aerospace

Boeing/Airbus deliveries & guidance*  
* 2015 is a management estimate

- Boeing/Airbus backlog >6000
- 787 launch backlog >800
- 737 monthly build increasing from 31 to 42
- A320 monthly build increasing from 36 to 44

High visibility of long-term growth

Passenger RPKs

CAGR GDP +4%

1990 2000 2010 2020
Power generation

- New capacity forecast to more than double from current low
- GE and Siemens comprise c60% of annual new capacity
- Shift to higher efficiency designs - GE 7H, 9H, LMS100

Growth ahead driven by forthcoming energy capacity shortfall
**Energy requirements drive exploration boom**

- Rig count forecast to grow 20% over next 3 years
- Non-US rig contribution growing from 40% to 50%
- US fracking/directional drilling driving advanced treatments

*Source: MB Strategy / Baker Hughes*
Bodycote leads the market

Broad spectrum of capabilities
- Surface coatings
- Hot isostatic pressing
- Metal joining
- Full heat treatment portfolio

Expansive accreditations & approvals list
- Nadcap (key aerospace approval)
- Norsok (key oil & gas approval)
- AMS (Aerospace Material Specification)
- All key OEM approvals

Meeting the needs of ‘majors’
- Capacity to meet peak requirements
- International footprint
- Risk mitigation – service redundancies
In summary – secular growth

- Aerospace & energy set for good growth, even if economy is turbulent
- Bodycote has strong leadership position
- Recent events:
  - New 10 year agreement with Rolls-Royce
  - 787 deliveries now underway
  - Investments to increase capacity
Emerging Markets
Emerging markets – where we are

2011 H1 Proportions

Largest
- Eastern Europe
- Brazil

Fastest Growing
- China
- Mexico
- Turkey

Strategic Outposts
- India
- Singapore

Emerging markets – today 10% of Group sales
28 plants in 11 countries
Emerging markets

Competitive advantage

- Partnership with established Western customers
- Global knowledge of customers and products
- Proven technology transfer capabilities
- Market leadership – here for the long haul
- Bodycote management system
- Comprehensive quality accreditations
- Long-term agreements, strategic partnering
Bodycote positioning

Partnering with global tier-1 and tier-2 component manufacturers requiring western-quality metal processing
Emerging market expansion strategy

Build plant clusters – hub and spoke model
- Establish linked plants in same region
- Build on success
- Immediate growth
- Rapid break-even

Preferred to:

Lone greenfield:
- Many challenges
- Several years of losses

Acquire – and reshape:
- Much quicker
- Costly/risky
- Reposition to higher value Bodycote work
- Withdraw from marginal activities
Hub & Spoke development cycle

a) Begin working with 2-4 new customers
b) Develop and prove prototype capability
c) Run initial production in hub
d) Build new satellite plant
e) Move customers from hub to satellite
f) Replace customers in hub and repeat
g) Add other customers local to satellites
Developing our established territories

Well established
- China
- Czech
- Hungary
- Poland
- Romania
- Turkey

Growing and good profits
- Develop existing clusters
- Add new plant clusters
- Main focus on China

Restructuring complete profitable and growing
- India
- Singapore
- Add high-value sales & incremental capacity

Work in progress
- Brazil
- Add high-value sales

Emerging Markets
In summary...

Today:
- 29 plants
- 10 countries
- Encouraging profits
- Good growth

Next:
- Build out plant clusters
- Focus on China

Stronger growth ahead
Changing Technology
Technology change

Customer technical needs are changing

Environmental legislation forcing change

Examples of new Bodycote technology to meet customers’ changing technical needs

2 new processes explained
European directives restrict use of Chrome VI

- Hexavalent chrome – Chrome VI – is a known toxin
- EC directives protect drinking water from Chrome VI pollution by waste recovery requirements
- Redesign of machinery and cars eliminates passivated zinc and electroplated chrome

Favours nitrocarburising with post-oxidation (proprietary Bodycote Corr-I-Dur® process)
Corr-I-Dur®

Superior corrosion resistance

- Process unique to Bodycote
- Eliminates Chrome VI – corrosion protection benefits
- Automotive and machinery applications

Brake piston
(280gm v prior 440gm)

60hr salt spray test vs chemical coatings

Hydraulic equipment pistons
Corr-I-Dur®

Complex, precise, high value process

- Multi-layer protection
- Adds nitrogen, then oxygen
- Cycle time: 12-20 hours

Diagram showing gas circulation, heat resistant retort, charging framework, and vacuum pump set with process control and gases including N₂, O₂, NH₃. Graph indicating 14-16 process steps.
Average CO₂ emissions/car

EU legislation:
- 130 gms by 2015
- 95 gms by 2020
- Lower than Smart car (97 gms)

Easy wins: already happened
Next steps: more technology, lower weight

More technology:
- Energy recovery, hybrids, advanced injection, turbo

Lower weight:
- Smaller mechanical components

More heat treatment
Classical carburising v new LPC technology

Low Pressure Carburising – similar process, but under vacuum
Low pressure carburising

Many advantages...

...for the environment
- Lower emissions

...for Bodycote
- Shorter cycle – more throughput
- Lower energy use

...for customers
- Improves fatigue behaviour and distortion
- Clean surfaces (even blind holes)
- No need for grinding
- Stronger lighter plants
In summary – technology change

Customer needs impacted by legislation:
- Elimination of Chrome VI
- Improved CO₂ emission
  - more technology
  - stronger, smaller parts

New Bodycote solutions – examples:
- Corr-I-Dur®
- Low Pressure Carburising

- Growing heat treatment requirement
- Particularly for new high-added value Bodycote processes
HIP Product Fabrication
The opportunity

- Penetrating market for:
  - Low-volume large complex parts
  - With optimum mechanical strength

- The market is currently served by top-end forgings
  - we estimate the market size for stainless steel forgings at €1 billion.
Product fabrication process

- Powdered alloy
- Design capsule
- Manufacture capsule
- Powder fill capsule
- HIP
- Heat treatment
- Inspection
- Finished product
- End application
Hot Isostatic Pressing (HIP)

Process
- Heats up to 2000°C
- Compresses up to 300 MPa
- Inert gas – Nitrogen or Argon
- Processes for up to 30 hours

What does the process do?
- Consolidates alloy powders to 100% solid metal
- Eliminates porosity in microstructure of components
- Improves mechanical properties - fatigue, strength, wear qualities

Completely different from Sintering
- HIP product fabrication is a high pressure process giving ultimate qualities. Sintering is a mass production process for producing low cost product.
Market segments & applications

- **Energy – Oil & Gas**
  - Valve bodies, pump housings, swivels, tees, hubs, manifolds

- **Machinery**
  - Extrusion barrels

- **Tooling**
  - Bars (solid and hollow), rectangular blocks, billets

- **Electronics**
  - Sputtering targets for flat panel display, semiconductors

- **Power generation**
  - Steam chests, rotors, turbine discs, rings, valve bodies
Advantage vs other fabrication methods

Near-net shape HIP PM was used to manufacture superconducting dipole cryomagnet end covers for the world’s largest energy subatomic particle accelerator known as the Large Hadron Collider.

### CERN comparison of critical criteria for four fabrication techniques considered

<table>
<thead>
<tr>
<th>Key: ++ very good, + good, - poor, -- very poor</th>
<th>Welded</th>
<th>Closed die forged</th>
<th>Cast</th>
<th>HIP PM</th>
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<td>Near-net shaping</td>
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<td>Reliability, Non Destructive Testing</td>
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Photo courtesy of CERN

Winner: Design Excellence Award Grand Prize

Photo courtesy of Metso
Barriers to entry

- **Know-how:**
  - Substantial know-how required
  - Both art and science
  - Our HIP knowledge established over decades
  - Includes design and modelling of complex shapes

- **Investment:**
  - HIPs are very expensive – a large HIP costs > £10m
  - Bodycote has 50 of varying sizes in multiple locations

- **Leadership:**
  - Bodycote the natural supplier with first mover advantage
Global leader

55% global market share (excluding captives)

10 HIP VESSELS

US & EUROPE
HIP Product Fabrication – the future...

Bodycote is:

- Well ahead with missionary selling task
- Establishing key customer partnerships
- Developing know-how for different applications
- Investing in resources and capacity

Current growth:
> 50% p.a.
S³P – Specialty Stainless Steel Processes
What is stainless steel?

- Steel alloy with minimum 12% chromium content
- Chromium oxide provides the corrosion resistance
Corrosion is costly

Friction, wear and corrosion of steels, including consequential losses, is estimated to cost 5% of European GDP.
Market analysis – stainless steel

Stainless steel production worldwide:

- 31m tonnes (2010)
- 6% CAGR over last 5 years

We process a minute share of total stainless steel

> Growth in 2011 H1 c.50%
Characteristics of stainless steel

- Many excellent characteristics – particularly corrosion resistance

- But... disadvantages:
  - Low strength
  - Low surface hardness
  - Low wear resistance
  - High risk of adhesion

$S^3P$ solution

Overcomes disadvantages
S³P offering

- Enhances...
  - Wear resistance 3x and more
  - Surface hardness 5x
  - Avoidance of sticking

- Overcomes weaknesses of stainless steel better than alternatives

- Several can harden – only we can maintain corrosion resistance

Unique, premium offering – for customers that need the best
**S3P offering – business concept**

- S3P is a solution provider
- Premium priced technology
- Missionary selling approach
- Highly diversified markets - worldwide

*Unique, proprietary product*
*Process has high price – but benefits justify cost*
S3P offering – locations

Track record:
> 5yr CAGR 17% despite economic crisis
> strong margins
Examples of S³P applications

**INDUSTRIAL FLUID & GAS HANDLING**

Key factors
- Large dimensions treatable ✔
- Increased wear resistance ✔
- Maintain corrosion resistance ✔
- Toughness at low temperatures ✔
- High reliability, reduction of lifecycle cost ✔

Applications ➤ pumps and valves
➤ connectors and fittings

**FOOD MANUFACTURING & PRODUCTION**

Key factors
- No risk of delamination v coating ✔
- No sticking of tight tolerance parts ✔
- Outperforms hard chrome plating ✔
- Wear resistant against abrasive foods ✔
- Maintain corrosion resistance ✔

Applications ➤ fluid handling
➤ bottling plant
Examples of S\textsuperscript{3}P applications

### AUTOMOTIVE

**Key factors**
- Highly resistant to surface wear ✓
- No post treatment machining required ✓
- Withstands modern fuel concepts ✓
- High reliability, provides longer part life ✓

**Applications**
- Turbo charger
  - Exhaust circulation
  - Variable camshaft system

### MEDICAL DEVICES

**Key factors**
- Biocompatibility ✓
- Maintains sharp edge during operation ✓
- Non-magnetic behaviour is maintained ✓
- Maintain corrosion resistance ✓

**Applications**
- Fixation instruments
  - Bone cutter
  - Implants
S³P actions

- 50% more capacity by end 2012
- Increase penetration of existing markets
- Continue missionary selling
- Expand into emerging markets in due course
Opportunity for substantial growth
Outstanding margins
Niche process – wide market applications
Growth & Resilience
Scoping the growth opportunities
The possibility of a downturn
Modelling some hypothetical scenarios

David Landless, Group Finance Director
Median case growth scenarios – 5yr horizon

<table>
<thead>
<tr>
<th>Growth Elements</th>
<th>GDP</th>
<th>1%</th>
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<td>Share of Gp. Sales</td>
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<td>Growth Premia</td>
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<td>Secular market growth</td>
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<tr>
<td>Changing Technology</td>
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<tr>
<td>Emerging markets</td>
<td>10%</td>
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<tr>
<td>Proprietary technology</td>
<td>20%</td>
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<tr>
<td>Out-sourcing</td>
<td>1%</td>
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<td>Discount</td>
<td>-2%</td>
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<tr>
<td>Bodycote growth</td>
<td>6%</td>
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Median case revenue – reality not a single line

5 year revenue model

Bodycote median case 6%
Prospects

- Possibility of a “double dip” impacting the general market
- Next slides provide historical context to scale of possible downturn
- And show our increased resilience

Secular Aero & Energy growth + 4 growth initiatives =

- “Premium growth” of 5% to general market
- Discounted to 3%
The long view

Year on year HT industry output change – at constant prices*

- 2009 truly exceptional 26% decline
- Typical cycle: a decline of 5 -10% once in 10 years
- 25 year CAGR: 3% at constant prices 5% at actual prices

History: - CAGR 5%, “Single digit” shock every 10 years
- 2009 impacted by co-incidence of exceptional events

*Source: US Federal Reserve – Heat Treatment & Coatings
US auto industry output – 25 years by quarter

Source: Federal Reserve

2009 crisis unique
- Auto production troughed at 40% of prior level
- GM bankruptcy and crises at other US majors
Boeing build units & PCC sales by quarter

Source: Boeing and Precision Castparts

Boeing production halt impacted suppliers in following year

Disruption to Boeing supply chain followed 2008 strike
Supply chain also impacted by 787 development traumas (& A380)
Supplier demand slumped c20% despite buoyant end-market
Industrial production – incidence of downturns

Source: US Federal Reserve data for industrial production - 25 year history

**Industrial production**

- Trend growth 2%
- Deviations from trend growth:
  - 2009 crisis 13%
  - 4 shortfalls of 2-6%
  - 3 shortfalls <2%

**Bodycote**

- We’ve evaluated a 10% deviation from trend
- Why 10%:
  - Worst crisis* in last 25 years save for 2009: 6%
  - Multiplier for our mix: \( x1.6 \) 10%

* 2001
Hypothetical scenario - 10% downturn from trend

5 year revenue model

Bodycote median case 6%

Economic downturn -10%
Bodycote has substantial infrastructure and fixed costs – and modest direct costs

High drop through:
- benefits incremental sales
- hurts “decremental” sales

Cost analysis at H1 2011

Bodycote business model - natural high operational gearing
### Profit effect of sales drop

| Aero & Energy | Auto & General 
<table>
<thead>
<tr>
<th>US/UK bias</th>
<th>Industrial</th>
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<tbody>
<tr>
<td>Europe</td>
<td>US &amp; ROW</td>
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</table>

Effect on profit of sales drop of 100:

- **After 1 week**
  - Aero & Energy: 90
  - Auto & General: 90
  - US/UK bias: 90
  - Europe: 60
  - US & ROW: 90

- **After 3 months**
  - Aero & Energy: 60
  - Auto & General: 70
  - US/UK bias: 60
  - Europe: 70
  - US & ROW: 60

- **After 9 months**
  - Aero & Energy: 50
  - Auto & General: 45
  - US/UK bias: 40
  - Europe: 45
  - US & ROW: 40

- Impact of sales drop in AGI less than impact of same drop in ADE
- Takes longer to achieve cost reductions in Europe
Cost profile in different scenarios

- **Normal steady growth**
  - Fixed
  - Semi-variable
  - Variable
  - Margin

- **Hypothetical sudden downturn**
  - Fixed
  - Re-aligned over several months
  - Variable
  - Margin

- **Cost gearing beneficial in growth scenario**
- **If sudden downturn occurs semi-variable cost re-alignment takes several months**
- **Ability to respond quickly greater than in 2008/9:**
  - temporaries 15.6%
  - previously 11.6%
Hypothetical Scenario: 10% downturn

Bodycote growth offset by downturn

- More resilient than in prior downturns
- Margins in this hypothetical scenario dip to c.12%
Cashflow resilience – EBITDA utilisation

Status quo:
- Net cash generation 8% to sales

Growth scenarios:
- Capex 1.2x to 1.5x depn.
- Significant net cash generation

Economic setback scenarios:
- Capex 0.6x depn.
- Still significant net cash

<table>
<thead>
<tr>
<th>Cashflow Scenarios</th>
<th>% to Sales</th>
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<tr>
<td>Current</td>
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</tr>
<tr>
<td>Growth 10%</td>
<td>10%</td>
</tr>
<tr>
<td>Growth 20%</td>
<td>20%</td>
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<tr>
<td>Downturn 10%</td>
<td>10%</td>
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- Net cash gen
- Dividend
- Tax
- WC & Legacy
- Growth capex
- Base capex

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<th>EBIT Margin</th>
<th>15%</th>
<th>17%</th>
<th>19%</th>
<th>12%</th>
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<tbody>
<tr>
<td>EBITDA Margin</td>
<td>23%</td>
<td>26%</td>
<td>28%</td>
<td>20%</td>
</tr>
<tr>
<td>Capex/Depn</td>
<td>80%</td>
<td>110%</td>
<td>140%</td>
<td>60%</td>
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Scenario:  Median case 6% 5yr CAGR

Bodycote median case 6%

Revenue

Margin
Recap

Secular Aero & Energy growth + 4 growth initiatives = “Premium growth” of 5% to general market
- Discounted to 3%

Return to high teen margins

Cash generation transformed – now minimal borrowings
Growth & Resilience – a recap

Stephen Harris, CEO
Bodycote has changed

Rear view mirror – prior to 2009:
- Network expansion
- Substantial investment
  BUT...
- Cash generation weak
- Business quality patchy

Now:
- Withdrawn from low margin business
- Focus on business quality
- Bench strength enhanced
- Margins starting to climb above the 10 year plateau
- Cash flow transformed
- Targeting premium growth
Much more resilient than 2008/09

Then

- Problem sites
- Boeing distortions
- US auto industry near death experience
- 13% falling to 2%
- Legacy overhang
- Marginal
- High

Now

- Varied growth engines
- Secular Aero/Energy growth
- Low double digits to high teens
- Much lower
- Strong
- Minimal
Above market growth aspirations

- Median case: Achieve 3% growth in excess of general market growth over next 5 years
- In high quality business
- No precision to the numbers
- Achievement will be uneven
- Route may well be bumpy

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Quantified some turbulent scenarios

What we know:

- Not yet back to 2007 activity
- Good current growth rate
- History shows 5-10% setbacks every 10 yrs or so
- 2009 suffered from extreme distortions
- P&L impact of a downturn

What we don’t know:

- Timing or magnitude of any prospective economic downturn
A changed Bodycote

- Bodycote targeting good growth but also able to withstand a downturn
- Robust margins
- Enhanced return on capital
- Good cash generation
Growth & Resilience

Stephen Harris, CEO