Smiths HY2025 Financial Results

Tuesday 25th March 2025

Opening Remarks

Roland Carter

Chief Executive Officer, Smiths Group

Good morning everyone and thank you for joining us today. I'll start by providing a few opening remarks before handing over to Julian to walk us through the first half numbers.

I'll then come back to you to provide an update on the strategy. And we'll have plenty of time at the end for questions.

Opening remarks

Strategic actions underway to unlock significant value and enhance returns to shareholders

As I said in January, since becoming CEO this time last year, the Board and I have been evaluating the options to maximise shareholder value. Despite making substantial progress with improved performance, the Group still trades at a discount to our expected valuation.

To address this we will focus on our high-performance technologies for efficient flow and heat management through John Crane and Flex-Tek; and separate Smiths Interconnect via a sale, followed by Smiths Detection via either a UK demerger or sale.

In parallel, we have increased our share buyback programme to £500m, and will return a large portion of disposal proceeds to shareholders.

As we execute this strategy, we will become a more focused business with a higher quality financial profile that has ample potential for growth and very significant value creation.

We have made good progress since January and I'll provide more detail later.

Strong HY2025 financial results; FY2025 outlook reaffirmed

Turning to first half performance – we delivered a strong set of financial results with growth across all key metrics. We enhanced returns to shareholders; invested in attractive bolt-on acquisitions; and maintained our focus on safety.

Given this performance, I'm pleased to reaffirm our FY25 guidance, which we have raised twice since last September.

Before handing over to Julian, I want to say a few words by way of introduction since this is his first set of results - having been appointed CFO in February.

Julian has been at Smiths for more than 12 years. His financial and strategic roles, alongside his experience at Flex-Tek and Smiths Interconnect equip him well to be CFO, to drive forward the strategic actions, whilst maintaining financial control and discipline of the business. I'm incredibly pleased and fortunate to have him working alongside me, to create and deliver value.

With that, I'll hand over to him to talk through the numbers.

HY 2025 Financial Results

Julian Fagge

Chief Financial Officer, Smiths Group

Thank you Roland, and good morning everyone.

HY2025 – Continued strong financial performance

I'm happy to be presenting my first set of results and I'm pleased with the progress we've made in the first six months of FY25 delivering another strong financial performance.

Organic revenue growth was 9.1%.

Including acquisitions, this increased to 10.2%, with reported revenue growth of 6.7%, reflecting the impact of adverse foreign exchange.

We grew operating profit 12.6% on an organic basis, and 9.5% on a reported basis, resulting in margin expansion of 40 basis points to 16.7%, or 50 basis points on an organic basis. This is consistent with our full-year guidance.

This strong operating profit performance translated to 14% EPS growth, enhanced by lower tax and interest charges, and the benefit of the share buyback programme.

Cash conversion was good - at 94% - and ROCE reached a high of 17.1%, as we made efficient use of our capital.

Reflecting all of this, we are again increasing our dividend by 5% to 14.23 pence, which is supplemented by the £500m share buyback programme.

These positive results were delivered despite the cyber security event in January. I'm pleased to report that all critical systems are now up and running, with the only financial impact on results relating to John Crane which I'll cover later.

Extending our track record of organic revenue growth

Turning to the results in more detail and starting with organic revenue growth.

As you can see here, we are delivering consistent top line growth, within or ahead of our current medium-term target of 4-6%.

Continued operating margin expansion

Strong revenue growth translated into even stronger operating profit growth with a 40 basis point reported margin expansion to 16.7%.

On an organic basis, margin expanded 50 basis points driven by:

- higher volume particularly in Smiths Interconnect and Smiths Detection; and
- continued price discipline, more than offsetting inflation

We delivered a net expansion of 30 basis points from efficiency savings, including the benefits delivered through the Smiths Excellence System, whilst continuing to invest in growth.

Offsetting these increases, we had a 60 basis point contraction from mix. This covers both business mix, with a higher growth coming from our lower margin businesses, and product mix mostly within John Crane and Flex-Tek.

Strong EPS growth driven by operating performance

Strong operating growth translated to an even stronger EPS growth of 14%. The impact of organic profit growth, lower tax and interest, accretive acquisitions and the share buyback together delivered 19.3% constant currency EPS growth. We have provided full year guidance on tax, interest and FX in the appendix.

Improvement in cash conversion

On operating cash, we generated £254m, a 94% conversion, up from 89% this time last year. This reflects ongoing disciplined working capital management, whilst continuing to invest in the business.

Full year capex is now expected to be around £100 million, down from the prior guidance of £110 million given timing changes, and higher versus last-year largely due to the investment programme in automation and capacity in John Crane.

Finally, operating cash performance translated to £143 million of free cash flow, up nearly 30% on last year.

Business Update

Turning now to the businesses, I'll talk first through John Crane and Flex-Tek – the businesses we will retain. And then, I will cover Smiths Detection and Smiths Interconnect, the businesses we will separate to unlock value.

John Crane – strong Q1, Q2 growth constrained by cyber incident; order book supports H2 outlook

John Crane delivered 3.8% organic revenue growth, against a strong prior year comparator when we grew 12.7%. Performance was constrained by the cyber incident where recovery took longer due to the number of systems involved.

Growth was led by strong original equipment sales, particularly in Energy, which although having a lower margin in the short-term, secures a long term, higher margin aftermarket revenue stream.

Operating profit grew 3.9%, with a 10 basis point organic margin expansion to 22.9%. This margin reflects disciplined pricing and efficiency benefits, whilst continuing to invest for future growth, offset by the negative impact of the lower margin OE sales.

We had significant wins in the first half in energy, including a third asset management contract in Saudi Arabia and a partnership to supply seals to a ground-breaking supercritical CO2 project. We expect strong demand across the full energy spectrum to continue over the medium term as customers focus on driving efficiency and emissions reduction.

Looking ahead, we expect the second half growth to improve on the first half, supported by a robust order book and market demand. However, the cyber incident disrupted orders in January which continued into Q3, moderating our growth expectations for the full year.

Flex-Tek – solid growth and execution despite challenging market conditions in US construction

Now turning to Flex-Tek.

Revenue increased 2.5% organically, with acquisitions adding a further 4.4% to growth.

Flex-Tek's industrial segment grew 2.0%, with growth of HVAC products continuing despite a subdued construction market.

Aerospace grew 4.8%, as we executed on the strong orderbook driven by new aircraft builds.

Operating margin was 19.8%, down versus a strong comparator in FY24.

The margin performance reflects positive pricing, and the benefit of efficiency savings offset by product mix, with the prior year benefiting from high margin industrial heating contracts.

Looking forward, the timing and shape of the US housing market recovery will be a key driver for Flex-Tek into the second half. On a rolling 3-month basis, US new housing permits declined 3.1%, new housing starts were down 2.7% and builders' confidence remains negative. However, the market outlook continues to be supported by a shortage of housing stock, and we are well positioned to take advantage of the recovery.

For aerospace, we expect sales to remain strong, underpinned by a healthy orderbook.

Building on our successful track record with acquisition of Duc-Pac Corporation

Our strategy to create value in Flex-Tek with accretive acquisitions has continued during the half. In September, we announced the acquisitions of Modular Metal Fabricators and Wattco. Today, we announced the acquisition of Duc-Pac Corporation, a metal duct manufacturer based in Massachusetts, for £32m at an attractive multiple of 7.2 times EBITDA.

This acquisition is another step in building a nationwide integrated offer of metal duct products in the HVAC segment expanding coverage into the north-east through an established brand and a well-run business.

Since the acquisition of Royal Metals, we have deployed a total of £270m of acquisition capital into Flex-Tek at a combined valuation multiple of 7 times, which together with a strong organic performance has compounded growth to 13.2% over this period and added 320 basis points of margin over the last 4 years.

Smiths Detection – significant volume growth in aviation; continued margin expansion

Now turning to Smiths Detection.

Revenue increased 15.3% organically, reflecting significant growth in aviation, partly offset by a decline in Other Security Systems.

Aviation growth of 28.7% was driven by the ongoing global rollout of checkpoint CT scanners. We have now sold more than 1,600 of our CTiX products, and continue to secure a good win rate of more than 50% of the units contracted to date. The programme is about halfway through, with another 2-3 years to run.

Other Security Systems revenue declined 11.3% against a high prior year comparator and reflected the phasing of certain contracts.

Detection's operating profit increased 23.2% and operating margin by 70 basis points, on an organic basis, reflecting the strong volume growth, along with improved pricing and efficiency savings.

Our strong order book supports a continued positive outlook into the second half, and beyond.

In September, we showcased our new X-ray diffraction product which will support future hold baggage upgrade programmes. It is currently undergoing certification in Europe.

Smiths Detection is also advancing its iCMORE software offer and was the first to receive approval from the Netherlands for its AI-driven detection system, an important addition to support growth in our higher margin aftermarket.

Smiths Interconnect – innovation and execution driving strong growth

Finally, Smiths Interconnect

Organic revenue growth was very strong at 26.8%, with growth across all business units. Aerospace & defence revenue grew 15.9% driven by the strength of innovation in our fibre optic, radio frequency and connectors products.

Growth in industrial markets was driven by an outstanding performance in our semi-conductor test business. This reflected a high programme win-rate, particularly in high-speed GPUs and AI-related programmes. Our technology leadership was externally recognised with a number of industry awards for our DaVinci 112 semi-test product.

The notably higher volumes as well as pricing, mix and significant benefits from efficiency programmes, drove an 80% organic increase in operating profit. This translated into a 510 basis point expansion in operating margin.

Looking ahead to the second half, we expect growth to continue, albeit at a more moderate rate.

Disciplined capital allocation with enhanced returns

Turning now to our capital allocation framework.

As we have previously communicated, we deploy capital to fuel organic growth, fund strategic and disciplined bolt-on acquisitions and return excess capital to shareholders – all of which we have demonstrated in the first half:

- Organically, we increased capex and invested in R&D and engineering to ensure sustainable future growth across all our businesses.
- We invested £97m in acquisitions in Flex-Tek at attractive multiples and accretive margins.
- AND we have enhanced our returns to shareholders, having increased the share buyback programme and raised the dividend

As of today, we have completed the initial £150m of the £500m share buyback programme, and are on track to complete the remaining £350m by the end of this calendar year.

In addition, we are committed to returning a large portion of disposal proceeds.

In summary, our balance sheet remains strong, giving us flexibility for FY25 and beyond to fund organic investment, undertake bolt-on M&A, and return capital to shareholders via dividend and buyback, all while maintaining our investment grade rating.

FY2025 outlook

And finally, a few words about our outlook for the rest of FY25.

We are reaffirming our twice-increased guidance of 6-8% organic revenue growth supported by good order book visibility and continued strong demand in our end markets, albeit with some uncertainty over the US construction market.

We are also reaffirming our expectation of a 40-60 basis point expansion in operating margin, driven by operational leverage and continued benefits from the Smiths Excellence System and other efficiency programmes.

This guidance reflects the current position of announced US tariffs and we continue to carefully monitor how the landscape evolves. Our largely local-for-local approach limits the impact as we typically source where we manufacture and manufacture where we sell.

We expect cash conversion for the full year to be in the low 90s percent.

In conclusion, we have delivered a strong first half financial performance. We have positive momentum towards meeting the full-year guidance, and we are focused on executing our strategy. With that, let me hand back to Roland.

Strategy Update

Roland Carter

Chief Executive Officer, Smiths Group

Strategic actions to unlock significant value and enhance returns to shareholders

Thank you Julian.

Let's turn to the strategic update. We have used the terminology 'FutureSmiths' to describe Smiths as it will be in its future state.

So, firstly I'll cover FutureSmiths, then move on to the new medium-term targets which are supported by the Acceleration plan and new business opportunities and I'll finish with an update on the separation processes.

FutureSmiths – focusing on our world-class John Crane and Flex-Tek businesses

FutureSmiths will focus on our John Crane and Flex-Tek businesses. 54% of the business is exposed to the General Industrial market, of which around half is construction, 38% to energy and the remaining 8% to aerospace. Combined, these businesses generated £1.9bn in revenue in FY24, with a pro-forma operating profit margin of 19.5%.

FutureSmiths – engineering a better future

The purpose of Smiths – engineering a better future – continues. FutureSmiths is a specialist engineering business focused on high performance technologies for efficient flow and heat management.

Our exposure to the three key markets of general industrial, energy and aerospace all present attractive growth opportunities over the near and longer term, underpinned by important mega trends.

FutureSmiths has long-standing, valued customer relationships - with the reliability and quality of our products proved through many years of serving our customers. We work in partnership with them to design products and solutions that address some of their most critical problems.

We operate in a coherent business model, with an embedded approach to operational excellence - the Smiths Excellence System. With the benefit of a simplified structure in the future, we will maximise the opportunity to streamline the cost base and upweight the role of our shared business support services further.

FutureSmiths will deliver sustainable growth through a combination of strong market positions, long-standing customer relationships and engineering domain expertise. This growth will drive high returns and good cash generation with low capital intensity.

Attractive and complementary business models, industry characteristics and financial performance

The two businesses have complementary business models, industry characteristics and value creation opportunities.

Their end markets benefit from very supportive growth trends, with the increased demand for energy efficiency and emission reduction a common theme for both.

John Crane derives a substantial proportion of its revenue from aftermarket, which is captive for the life of the seal. Flex-Tek also has a significant recurring revenue stream with more than 90% repeat business, supported by its well-established OEM and distributor relationships, as well as its reputation for innovation and product performance.

Both businesses have expansion opportunities – geographically as well as into attractive product and service adjacencies.

All of these attributes support the significant potential for further growth and value creation.

Enhanced financial performance of FutureSmiths

As is evident here, FutureSmiths has a higher quality financial profile, with a strong track record of organic growth, high margins and returns in excess of our current medium term targets and good cash conversion.

Enhanced medium-term targets – reflecting further growth and higher return potential

Off the back of this strong financial profile coupled with further opportunities for growth and improved profitability, we have issued new enhanced medium-term targets for FutureSmiths.

We have upgraded our organic revenue growth expectations to 5-7%, increased EPS growth to greater than 10%, and raised operating profit margin to 21-23%.

All this will be achieved whilst maintaining disciplined capital management, with our return on capital employed target increasing to greater than 20%, and maintaining operating cash generation of around 100%.

We believe these ambitious, yet achievable targets support a premium rating for FutureSmiths.

Clear plan with focused execution agenda underpin growth and value creation ambition

Here we demonstrate the clear roadmap to delivering enhanced organic growth and further improving profitability supporting these new medium-term targets.

The value creation opportunities for John Crane and Flex-Tek are shown as well as highlighting the opportunities for cross-business collaboration in products, market and customers to augment future growth. We also see significant organisational and process opportunities, for example through shared support services, to deliver a streamlined cost structure within and across the businesses.

Medium-term margin expansion supported by Acceleration Plan

Turning to our Acceleration Plan where we have made good progress.

As you will recall from September, the plan is about value creation, not just transformation, and each business has a specific set of actions. These initiatives will deliver end-to-end process improvements for resilience and scalability over the longer-term, as well as specific cost reduction and footprint rationalisation actions. The plan also includes the right-sizing of Group central costs in line with the portfolio changes.

We continue to refine the focus and timing of the programme and are now expecting to deliver £40m-£45m in annualised benefit for the £60-£65m cost previously communicated. Costs will now be £20-£25m this fiscal year with the remainder in FY26.

Around two-thirds of both the costs and benefits relate to FutureSmiths. This includes the reduction in central costs, which, following completion of the separation processes, will be 1.5-1.7% of revenue, continuing to be at a more efficient rate than the median of our UK industrial peers.

The Acceleration Plan is just one lever to drive margin towards our 21-23% target – supported also by operating leverage and ongoing efficiency savings through SES, whilst continuing to invest in growth.

Separation of Smiths Interconnect and Smiths Detection initiated

Since the announcement in January, we have commenced the separation processes. Advisers have been appointed and we remain committed to the timetable of an announcement for Smiths Interconnect before the end of this calendar year, with Smiths Detection to follow.

Both Board and Executive Committees have been established to oversee the separations, ensuring governance and delivery at pace, with accountability.

We are conscious that the proposed changes are unsettling for our people and are committed to treating all our stakeholders respectfully as we go through this transition period.

And we are committed to separating responsibly with a focus on maximum value creation.

Smiths Interconnect and Smiths Detection – strong, well-performing businesses in attractive markets

As Julian set out earlier, we have seen strong performance this half from both Smiths Interconnect and Smith Detection, positioning them well for the second half and beyond.

Having run these businesses prior to our current roles, both Julian and I know them well. They share many of their key strengths with John Crane and Flex-Tek; leading technologies, strong positions in attractive markets and customer intimacy.

For example, Smiths Interconnect partners with customers to meet some of the most demanding specification, with strong capabilities in specialist applications such as optical transceivers for use in aerospace and defence, or semi-test sockets for AI chips. Smiths Detection is clearly a leader in threat detection with a global service reach.

However, their financial profile in regard to margin and returns is different from that of John Crane and Flex-Tek. They both have inherent opportunities to create additional value - through product development and expansion as well as efficiency improvements – we believe that these will be best delivered under different ownership and now is the right time for separation from a position of strength.

Summary – compelling opportunity to deliver significant shareholder value

So in summary,

All businesses contributed to the strong 9.1% organic revenue growth in the half, and we are reaffirming our 6-8% guidance for the full year.

John Crane and Flex-Tek have a strong track record of delivering through-cycle growth, and are well positioned in attractive markets to achieve enhanced organic revenue growth.

We increased the operating profit margin to 16.7% and are reaffirming full year guidance of 40-60bps expansion. We will continue to execute our Acceleration Plan to support further margin expansion beyond this year, and are committed to being ambitious as we embark on right-sizing our central costs.

We continued to invest in R&D and, through M&A, further expanded our reach in Flex-Tek. We increased the interim dividend by 5% and have completed the first £150m our share buyback programme, with the remaining £350m to be completed by the end of this calendar year. And we are committed to returning future disposal proceeds.

Our strategic actions are underway. We believe now is the right time to optimise the portfolio and focus on John Crane and Flex-Tek.

We have initiated the process to separate Smiths Interconnect and Smiths Detection.

We firmly believe these strategic actions will unlock significant value and enhance returns to shareholders.

I would like to acknowledge our employees and thank them for contributing to the strong financial performance in the half, and for their continued hard work despite the backdrop of a cyber incident and the recent newsflow. Your commitment is very much appreciated and not taken for granted.

So now let’s go to questions.