DE LA RUE PLC REPORTS 2015/16 ANNUAL RESULTS

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Sale of CPS

On 23 May, one day before reporting the 2015/16 year-end results, De La Rue announced the long expected sale of Currency Processing Solutions Ltd (CPS) to Privet Capital, a UK-based private equity firm specialising in buying underperforming businesses and turnaround situations. The senior team of Privet Capital includes the founder and Managing Partner, Steve Keating, and Chris Hyman, the former Group CEO of SERCO, the FTSE 100 security service provider Serco.

From being the market leader of banknote sorting machines in the early 1990s, De La Rue's CPS business faced fierce competition from both Currency Systems International (CSI) and Giesecke & Devrient (G&D), which resulted in the acquisition of CSI in 2001 and the consolidation of its sorter technology largely on CSI's CPS platform. De La Rue has always maintained the position that CPS activities are key to its currency business, with design, production, detection and processing of banknotes being links of the same value chain. CPS was viewed as a vehicle for gaining a better understanding of its customers' needs, a way to expand the market to include commercial cash handlers, even a lever to influence banknote security feature selection based on its detection and automated processing capabilities: in essence, a key differentiator against its competitors by offering full vertical integration of its banknote proposition – and particularly a defence against its main competitor, G&D, who would otherwise gain a foothold with its traditional banknote customers. Financial performance of the division fluctuated in and out of profit, and in 2015/16 resulting in a c.£8m loss.

De La Rue has received £2.1m upon completion of the sale, with a further deferred payment of £1.5m payable in the next 2 years. There is also a contingent sum of £6.5m in the event of reaching certain performance targets, but at this point it is difficult to assess the likelihood of this future payout. Overall, the transaction is viewed by De La Rue as cash neutral.

For comparison, the earlier spin-off of De La Rue cash desktop and dispensing/recycling devices business, which later became Talaris and is now a part of Glory Global Solutions, was sold in September 2008 for £360m to Carlyle Europe Partners, an alternative asset management group, who subsequently sold it to Glory Ltd. in 2012 for £650m. Under Carlyle's ownership the earnings of Talaris increased by more than 40% and its market presence expanded to more than 100 countries.

The main financial impact of the CPS sale (estimated profit on disposal between £nil and £3m) will be reflected in next year's results, but its timing permitted De La Rue to separate the loss-making discontinued operations while presenting 2015/16 performance, showing more positive reported figures for the ongoing business.

For De La Rue the sale has resulted in a £23.4m impairment charge, of which £17.8m relates to inventories. Considering how infrequent sales of high-speed sorters are this amount of inventories is somewhat surprising.

De La Rue's main competitor G&D appears to be able to exploit successfully the advantages of being a supplier of hardware and software to Central Banks with its currency operations, albeit, admittedly, with a much larger market share in high-speed sorters than that of De La Rue. Whilst the sale does include CPS maintaining a strategic partnership with De La Rue, it remains to be seen whether it will bring benefits to De La Rue beyond a short-term removal of a loss-making part of the business.

For the new CPS company, this offers a real opportunity finally to bring stability and focus to the business, but it will inevitably require dedicated investment and a strategic turn-around to be able to compete in the long-term with its main competitor.

The market reacted positively to the news of the CPS disposal, with share price gaining around 6% on the day of the announcement.

Performance of continuing operations

Consolidated 2015/16 year results as reported (unadjusted for the sale of CPS) show a small growth in revenues of 3% to £488m and a drop of -10% in profit to £62.5, mostly in line with the market expectations.

Once considered on the basis of continuing operations excluding CPS, De La Rue performance indicators in 2015/16 are largely positive. The revenue is up 7% to £454.5m and the underlying operating profit is up 2% to £70.4 from the year before. The 12 months order book is looking very healthy at £365m (of which £278 are in the Currency division), a marked improvement of 62% year-on-year.

Both currency and paper volumes are up, 9% and 6% respectively, although the operating profit margin in the Currency business has declined marginally by 30 basis points, from 15.9% to 15.6%, which is not unexpected in the continuing industry overcapacity climate. The growth in currency volumes is explained by overspill orders from SPWs.

De La Rue is continuing to optimise its production capacity, aiming to reduce its own annual banknote printing capacity to around 6bn, a 25% reduction from the original 8bn. Additionally, it plans to have access to c.1bn printing capacity at strategic outsourcing partners, and so far this has proven successful, with around 500 million notes outsourced in 2015/16. This understandably raises a question of the impact of outsourcing on the profit margin, and whether the capacity reduction, incurring considerable restructuring cost, will not be excessive, given that current De La Rue banknote print sales are already at 7.1bn notes, exceeding the combined own capacity and projected outsourcing volumes.

De La Rue continue to invest in R&D and justifiably sees polymer as a growth sector where it is well positioned to continue gaining a market share, being the only integrated currency printer in the market with just two banknote substrate manufacturers. So far the progress De La Rue makes with the sales of polymer notes has been encouraging, but profitability of this segment is yet to be established.

Comparison with Giesecke & Devrient

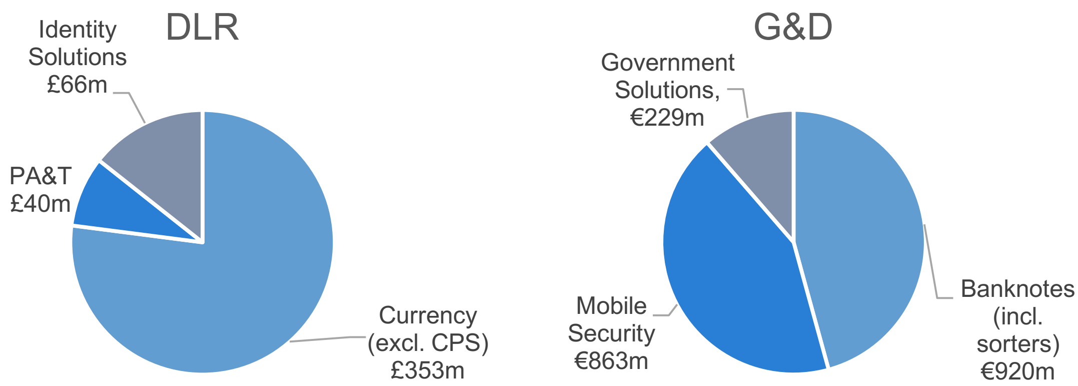
Financial summary[1]

	De La Rue			G&D		
	2015/16	2014/15	Y-o-Y change	2015	2014	Y-o-Y change
	GBP millions			*EUR millions*		
Sales	488.2	472.1	3%	2,010.9	1,833.1	10%
Profit before tax	**20.8**	**38.9**	**(47%)**	**79.8**	**(40.3)**	**nm**[2]
Add back Net finance cost	12.1	11.8		21.8	29.1	
Adj. for exceptional items	29.6	18.8		-	73.8	
Underlying operating profit	**62.5**	**69.5**	**(10%)**	**101.6**	**62.6**	**62%**
Depr'n & amortisation	26.2	24.8	6%	109.6	103.9	5%
EBITDA, home currency	**88.7**	**94.3**	**(6%)**	**211.2**	**166.5**	**27%**
Exchange rate, average for the period	*1.36*	*1.28*		*1.00*	*1.00*	
EBITDA, €	121.1	120.7	0%	211.2	166.5	27%

[1] Sources: De La Rue plc Preliminary Statement, Year to March 26 2016; G&D Annual Reports 2014 and 2015.
[2] Not meaningful

Both companies had a challenging time in 2014-2015 and spent considerable effort towards cost reduction and restructuring, but the recovery of G&D appears so far more robust than that of De La Rue.

Sales by business unit



Currency accounts for c.75% of De La Rue's total revenue, and less than half of G&D's.

Operational performance[3]

Margins (% of Sales):	De La Rue 2015/16	De La Rue 2014/15	De La Rue Y-o-Y change	G&D 2015	G&D 2014	G&D Y-o-Y change
Profit before tax	4.3%	8.2%	-398bpts	4.0%	-2.2%	+617bpts
Underlying operating profit	12.8%	14.7%	-192bpts	5.1%	3.4%	+164bpts
Depr'n & amortisation	5.4%	5.3%	+11bpts	5.5%	5.7%	-22bpts
EBITDA	18.2%	20.0%	-181bpts	10.5%	9.1%	+142bpts

[3] SMI calculations based on the reported financial statements. All margins are shown as percentage of sales.

De La Rue continues to achieve significantly better profitability than G&D on average across all business units. Despite this, De La Rue figures are deteriorating while G&D are mainly improving.