

19 March 2015

## Coats Group plc

### Annual Financial Report 2014

Coats Group plc ('Coats' or the 'Company') has today submitted to the Financial Conduct Authority's national storage mechanism its Annual Financial Report for the year ended 31 December 2014 ('Annual Report 2014'), as required by UK Listing Rule 9.6.1.

The Annual Report 2014 is available to view on the Company's website, [www.coats.com/AR2014](http://www.coats.com/AR2014), and will also be available for viewing at the Financial Conduct Authority's national storage mechanism at [www.morningstar.co.uk/uk/NSM](http://www.morningstar.co.uk/uk/NSM).

The Company has also released a PDF copy of its Annual Report 2014 to the New Zealand Stock Exchange and Australian Securities Exchange.

This announcement also contains as appendices additional information for the purposes of compliance with the UK Disclosure and Transparency Rules, including principal risk factors, details of related party transactions and a responsibility statement. This information is extracted, in full unedited text, from the Annual Report 2014. The Preliminary Announcement released on 26 February 2015 contained a condensed set of financial statements together with extracts of the Company's management report, and is also available to view on the Company's website, [www.coats.com/FY2014](http://www.coats.com/FY2014). These announcements should be read in conjunction with and are not a substitute for reading the full Annual Report 2014.

Stuart Morgan  
Company Secretary  
19 March 2015

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**Enquiry details**

UK media	Richard Mountain	+44 20 3727 1374
New Zealand and Australian media	Geoff Senescall	+64 9 309 5659
Investors	Jaideep Thatai	+44 20 8210 5086

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## Appendix

### Principal risks and uncertainties

A description of the principal risks that the Company faces is extracted from pages 6 to 7 and pages 18 to 19 of the Annual Report 2014.

It is the responsibility of the Board and its various committees to identify and understand the key risks faced by the business and to ensure mitigating action is taken to control them. Those risks are:

Risk	Nature of Risk	Action/Mitigation
Employee defined benefit obligations – accounting impact and regular funding	<p>The Group has a number of employee defined benefit arrangements in place, the most significant being:</p> <ul style="list-style-type: none"> <li>&gt; three UK pension schemes: Coats, Brunel and Staveley; and</li> <li>&gt; the Coats North America plan.</li> </ul> <p>The UK schemes can impact the Group on various levels. Given their size, and particularly that of the Coats Pension Plan, these schemes can have a material impact on the Group's reported results. Under IAS19 the Consolidated Income Statement includes an administrative charge and a finance cost relating to these schemes and variations in these charges can give rise to fluctuations in reported earnings. In addition, changes in the IAS19 accounting surpluses and deficits in the schemes impact the level of shareholders' funds.</p> <p>When funding deficits arise this can have a cash flow impact. The net accounting and funding positions of these arrangements are particularly sensitive to real discount rates and the investment performance of any segregated assets.</p>	<p>Managing the funding position of the three UK pension schemes is the primary responsibility of their respective trustees. The strategy followed by each trustee targets the long term funding position of its scheme. Each has used corporate bonds to fund short term liabilities. Equities and other return-seeking assets are held for the longer term. These provide a natural hedge respectively for short term obligations and long term inflation risk. Coats has in place a short term inflation hedging programme. In addition, the trustees have implemented formal de-risking strategies with thresholds for switching return-seeking assets into bonds.</p> <p>The 2012 funding valuation for the Coats UK Pension Plan was completed during 2013 and a scheme deficit of £215 million was agreed. As of November 2013 a 14 year recovery plan commenced and the rate of contributions increased from that date from £7 million per annum to £14 million per annum. In addition Coats plc agreed to provide the scheme with a parent company guarantee.</p> <p>The Brunel scheme is in the process of completing its 2013 triennial valuation. There was no deficit in 2010 and, hence, there is currently no recovery plan. However, the Board expects a deficit and a recovery plan to result from the current exercise.</p> <p>The Staveley scheme last had a triennial valuation as at 5 April 2011. The 2011 valuation resulted in a one-off payment of £5 million being made to the scheme in July 2012 and an eight-year recovery plan at an annualised rate of £1.3 million.</p> <p>The triennial valuation processes for both the Brunel and Staveley schemes are on-going and have been delayed by tPR's investigations. The Company is engaged in discussions with the trustees of both schemes with a view to reaching agreement on the valuations in due course.</p> <p>The Coats North America plan has a funding surplus and the investment strategy followed includes a matching asset pool which should substantially reduce the risk of a funding shortfall arising in the future.</p>
Employee defined benefit obligations – regulatory investigation	As previously reported and described further in the Chairman's statement on pages 3 to 4, tPR is investigating the Group's three UK defined benefit pension schemes and has issued Warning Notices in relation to all three schemes.	The Board continues to actively engage with tPR's investigations and will continue to explore all options to try to resolve these matters balancing the interests of all stakeholders.
Treasury concentration risk	The completion of the asset realisation programme combined with the deferral of the return of capital to shareholders during tPR's investigations has resulted in a significant proportion of shareholder value being represented by cash.	The Board is cognisant of the potential for this to give rise to concentration risk. The Board is provided on a monthly basis with a report of cash balances by bank, jurisdiction and currency. In addition it regularly reviews these risks at Board meetings to ensure appropriate mitigating action is being taken.

Foreign currency exposure	<p>Coats business' activities are primarily denominated in USD, although it has major asset bases in other currencies, including the Indian Rupee and the Brazilian Real.</p> <p>Coats takes action to protect its anticipated transactional currency exposure but does not hedge its assets and liabilities.</p> <p>Cash generated through the asset realisation programme is primarily held in GBP, USD and NZD. The GBP balance is held to cover known liabilities whereas the NZD and USD balances represent the currently surplus funds.</p> <p>Given the investigation being carried out by tPR, the Board faces the potential of some as yet unquantified obligations to provide further financial support to the Group's UK pension schemes. The size and nature of these obligations will only be known once the process with the respective scheme trustees and tPR has been completed. Any hearing before the Determination Panel of tPR for all three schemes is unlikely before the second half of 2016 at the earliest. If all rights of appeal are pursued, this process would extend beyond this period.</p> <p>This in turn means the Board is currently not able to determine with certainty the quantum of future returns, if any, to shareholders.</p>	The Board regularly reviews its currency exposures and has taken steps to ensure transparent reporting to shareholders of the positions held.
Human resources	Shareholder value is heavily dependent on key individuals within the Group.	The Board has recognised the risk to delivery of the Company's strategy from key staff leaving during the process. It regularly reviews the appropriateness of its incentive and reward arrangements and has established retention and/or incentive plans to address this risk.
Coats	Given the simplification of the Company's business model, the Coats business now represents the major portion of the Group's business risk.	<p>Coats faces a wide range of commercial and operational risks. Coats manages these risks through various structures, including its Internal Audit Function and Operational Risk Management Committee, comprising a broad mix of managers across the business, chaired by the Group Chief Executive.</p> <p>The Head of Internal Audit attends meetings of and reports to the Board's Audit and Risk Committee. The key risk areas identified and managed through this process are described in more detail on pages 18–20.</p>

Coats faces a wide range of commercial and operational risks. While our risk management process is driven from Board level, identifying, assessing and managing risks is embedded into our day to day operations. Overlaying Coats' positive business principles and culture are formal structures and reporting procedures, including the Internal Audit Function and the Operational Risk Management Committee (ORMC), which comprises a broad mix of managers across the business and is chaired by the Group Chief Executive.

Risk	Nature of Risk	Action/Mitigation
<b>Strategy and strategic planning risks</b>		
Delivery of strategy	A lack of resource, poor project management, lack of skills or lack of acceptance in the market may result in not delivering growth projects. Consequently profitability goals are not achieved or the market multiple is materially below target.	<p>Projects are managed by a dedicated team and sponsored by a member of the Coats Management Board or Industrial or Crafts Americas Leadership Teams. They are controlled by a Steering Committee and monitored financially.</p> <p>The Board receives regular progress reports and sets targets for profitable sales.</p>
Recruiting, maintaining and motivating high-quality	Not identifying and retaining key staff or improving their skills and knowledge may result in an inability to execute growth strategy.	HR policies cover reward and recognition, health and safety, talent management, skills assessment and development, performance

staff		<p>management, succession planning and employee consultation.</p> <p>An annual group-wide employee satisfaction survey flags any areas for concern which are then acted on.</p> <p>An annual survey of pay and benefits ensures that terms and conditions of employment remain competitive.</p>
<b>Financial risks</b>		
Pension	Fluctuations in discount rates, investment values and returns, inflation and/or member longevity in the defined benefit pension arrangements result in funding burdens on the Group in the future.	<p>Pension position and strategy is regularly reviewed by the Board.</p> <p>Funded pension schemes are overseen by their trustees. Trustees are required to have the appropriate knowledge and understanding in this area and take professional and actuarial investment advice as necessary. Where appropriate independent professional trustees are appointed to schemes to provide additional expertise.</p> <p>Coats and the trustees seek to de-risk the scheme through liability management and investment strategies to reduce the impact of fluctuations.</p>
Treasury	An exposure to uncertainties in financial markets and the banking sector including foreign exchange, interest rate, credit and liquidity risks as well as the risk of bank failure.	Coats' policies cover all aspects of its Treasury operations, providing strict controls on managing risks and bank selection.
	Coats may be unable to present itself as an attractive candidate for financing.	Compliance with the terms of Coats' senior bank facility agreements is actively monitored. There is regular contact with core relationship banks and alternative sources of finance have been identified. In 2015 debt facility was successfully refinanced and maturity extended to 2020.
<b>Operational risks</b>		
Information Technology (IT)	Unauthorised access to Coats IT systems and data may result in the theft of data or the disruption of business processes.	<p>Standard firewall capability is overseen by an external vendor. Coats' networks are actively monitored and multiple layers of password protection are used at device and application level. Communications with portable devices are encrypted.</p> <p>Coats ensures all internal users have appropriate access rights and permissions for their roles.</p>
	An inability of Coats' IT network and systems to perform critical transactions and processes may result in business disruption.	Coats has sufficient network capacity and established IT systems in place with Group and Divisional IT teams to manage the IT risks.
Supplier dependency	If one or more major external suppliers is unable or unwilling to supply goods it may cause major disruption to the Coats supply chain that cannot be replaced in the shortterm, leading to lost contribution and longterm impact on customer relations.	<p>Supplier relationships and external supply chains are monitored and managed, with multiple sourcing of materials and strategic inventories.</p> <p>Regular supplier meetings include detailed discussions of market conditions and supply expectations. Risk is spread by dealing with more than one supplier on each key material and continual identification of new supply sources.</p> <p>Global insurance programmes include supplier dependency cover.</p>
Internal supply chain	Disproportionate reliance on critical internal supply chain nodes may have a significant impact on profitability in the event of disruption to any of them.	<p>Manufacturing and supply chain function monitors and reviews internal supply chains, fire protection systems and creates and tests disaster recovery plans.</p> <p>Rolling property risk surveys are conducted of all Coats critical supply chain nodes. The implementation of the risk reduction recommendations is actively monitored and where necessary capital expenditure is prioritised.</p>

		Global insurance programmes include property destruction and business interruption cover.
Customer dependency	Key Crafts customers reduce shelf space for a group of products which Coats supplies or engages in price negotiation, materially reducing the contribution earned by the business.	<p>Strong commercial relationships are maintained with senior level management with direct access to final decision makers. Coats works to ensure a high degree of customer collaboration, communication and management attention to POS data and weekly replenishment levels. It provides a high level of service/stock availability.</p> <p>Significant investment in pattern/design support, product promotions and consumer advertising undertaken to boost in-store footfall and sales growth. Strategic marketing has targeted craft consumer demographics, in-store buying behaviour and positive correlation to store sales in other categories.</p>
Environmental	Non-compliance with internal environmental control procedures or local requirements (if these are stricter) leads to a serious pollution event having an adverse impact on operations and resulting in regulatory action being taken. This results in litigation, resultant damages and damage to reputation.	<p>Management aims to achieve the highest practicable standards of environmental performance. All environmental issues are reported to the Group's Audit and Risk Committee and Management Board through a semi-annual Risk Questionnaire completed by all operating units.</p> <p>All sites must comply with local legal requirements for effluent quality and volume and hold the relevant permit to discharge. Coats has 'Global Water Effluent Limits', a set of 15 parameters with the strictest limits of any local authority across three downstream categories.</p> <p>Global insurance programme includes cover for 3rd Party property damage and injury or illness resulting from pollution of air, water or soil caused by a sudden or unforeseen incident.</p>
	Coats may be held responsible and accountable for clean-up/remediation costs of legacy environmental issues originating before it acquired those sites or after their disposal/closure.	<p>Appropriate checks are undertaken on sites we are looking to acquire, and we conduct ongoing monitoring of current sites.</p> <p>Every step appropriate is taken to ensure closed and/or sold sites are cleaned up.</p>
Labour relations	Poor labour relations in critical manufacturing sites could result in disruption to business.	<p>An annual Employee Engagement satisfaction survey is conducted and relevant strategies developed and implemented to address concerns.</p> <p>In the event of disruption, Coats can move production to other sites.</p>

### Related party transactions

A description of the related party transactions of the Company is extracted from page 88 of the Annual Report 2014:

#### Remuneration of key management personnel

The remuneration of the Directors, who are the key management personnel of the Group, is set out below in aggregate for each of the categories specified in IAS 24 – Related Party Disclosures. Further information regarding the remuneration of individual directors is provided on page 37 in the audited part of the Directors' remuneration report.

Year ended 31 December	2014 £m	2013 £m
Short-term employee benefits	1	1

#### Trading transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note. Transactions between the Group and its Joint Ventures are disclosed below.

During the year, Group companies entered into the following transactions with related parties who are not members of the Group:

	Sales of goods		Purchases of goods		Other income	
	2014 £m	2013 £m	2014 £m	2013 £m	2014 £m	2013 £m
Joint ventures	4	4	29	28	2	3

Transactions with Joint Ventures are conducted on an arm's length basis.

Amounts owing by/(to) Joint Ventures at the year end are disclosed in notes 19 and 21.

### Responsibility statement

The following responsibility statement is repeated here solely for the purpose of complying with Disclosure and Transparency Rule 6.3.5. This statement relates to and is extracted from page 41 of the Annual Report 2014. Responsibility is for the full Annual Report 2014 and not the extracted information presented in this announcement or the Preliminary Announcement released on 26 February.

We confirm that to the best of our knowledge:

1. the financial statements, prepared in accordance with International Financial Reporting Standards as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
2. the Strategic Report includes a fair review of the development and performance of the business and the position of the Company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

The Directors' responsibilities statement was approved by order of the Board.