PRELIMINARY ANNOUNCEMENT AND PRESENTATION 2012

BAE SYSTEMS

RESULTS IN BRIEF AND FINANCIAL KEY POINTS

Results in brief

	2012	2011
Results from continuing operations		
Sales[1]	**£17,834m**	£19,154m
Underlying EBITA[2]	**£1,895m**	£2,025m
Operating profit	**£1,640m**	£1,580m
Underlying earnings[3] per share:		
– including R&D tax benefit	**n/a**	45.6p
– excluding R&D tax benefit	**38.9p**	39.7p
Basic earnings per share[4]	**32.8p**	37.0p
Order backlog[1,5]	**£42.4bn**	£39.1bn
Other results including discontinued operations		
Dividend per share	**19.5p**	18.8p
Operating business cash flow[6]	**£2,692m**	£634m
Net cash/(debt) (as defined by the Group)[7]	**£387m**	£(1,439)m

Financial key points

- Sales[1] reduced by 7%
- Underlying EBITA[2] reduced by 6% to £1,895m. Deferred recognition of sales and profit relating to the formalisation of price escalation on the Salam Typhoon programme
- Underlying earnings[3] per share down by 2% (excluding the benefit in 2011 of the UK tax settlement)
- Order backlog[1,5] increased by 8% to £42.4bn
- Non-US and UK order intake[1] increased to £11.2bn from £4.8bn in 2011
- Total dividend increased by 4% to 19.5p
- Operating business cash flow[6] increased to £2.7bn
- Net cash[7] balance of £387m
- Three-year share repurchase programme of up to £1bn initiated
- Longevity risk on £2.7bn of pension scheme liabilities transferred to the insurance market

1 Including share of equity accounted investments.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 6).
3 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).
4 Basic earnings per share in accordance with International Accounting Standard 33, Earnings per Share.
5 Order backlog comprises funded and unfunded unexecuted customer orders, and is stated after the elimination of intra-group orders.
6 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.
7 See definition on page 7.

OUTLOOK

This outlook statement assumes US budgets are subject to Continuing Resolution for the first quarter of 2013 only and does not reflect the impact that might result from a US sequestration.

Subject to near-term uncertainties relating to US defence budgets, modest growth in underlying earnings[3] per share is anticipated for 2013. This excludes any benefit from the share repurchase programme in 2013. In addition, and assuming a satisfactory conclusion to Salam pricing negotiations this year, there would be a further increase of around 3 pence in underlying earnings[3] per share.

- Electronic Systems sales[1] are expected to be at a similar level to those in 2012 with margins expected to be slightly lower within a range of 12% to 14%.
- Cyber & Intelligence sales[1] are expected to be marginally lower than those in 2012 with margins expected to be within an 8% to 9% range.
- In Platforms & Services (US), Land & Armaments sales[1] are expected to be approximately 10% below the 2012 level with margins around 8%. Support Solutions sales[1] are expected to be marginally higher than in 2012, with slightly reduced margins.
- Platforms & Services (UK) sales[1] in 2013 are expected to increase by around 25%, assuming a price escalation settlement and resumption of aircraft deliveries on the Salam Typhoon contract. Margins are expected to be similar to those in 2012.
- Platforms & Services (International) sales[1] are expected to be marginally higher than in 2012. Margins are expected to benefit from the anticipated resolution of Salam Typhoon price escalation, and are expected to be at the top end of a 10% to 12% range.
- HQ costs are expected to be more than 10% lower than in 2012 and Group earnings[3] are expected to reflect marginally lower underlying finance costs. An effective tax rate within a 23% to 25% range is expected.

Notwithstanding cash inflows from an anticipated Salam price escalation settlement, significant cash utilisation is expected in 2013. This includes an expected high level of utilisation against the advances, received in 2012, on the Saudi trainer aircraft and Omani Typhoon and Hawk contracts and advances consumed on the European Typhoon production contracts.

1 Including share of equity accounted investments.
3 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).

PRELIMINARY RESULTS STATEMENT

BAE Systems has continued to deliver on a clear strategy during 2012. The Group's geographic breadth of business has provided, and is expected to continue to provide, resilience at a time when some of its markets are constrained by economic pressures. Following a period of growth, defence budgets in the US have flattened and are expected to remain constrained in response to reducing overseas operations and measures to address federal deficits. In the UK, the defence market has stabilised following changes to programme priorities outlined in 2010 through the UK government's Strategic Defence and Security Review.

Growth opportunities in some segments of the US and UK markets are identified, but the overall outlook in both countries is expected to continue to be constrained.

In wider international markets, the Group is seeing good growth in order intake leading to anticipated growth in international sales. In 2012, order intake outside of the US and UK was £11.2bn, compared with £4.8bn in 2011.

BAE Systems has a clear strategy, focused on enhancing its position as a premier global defence, aerospace and security company. Consistent with that strategy, discussions between BAE Systems and EADS were held between June and October of 2012. The discussions involved extensive engagement with many of the Group's government stakeholders, including in the UK, US and Saudi Arabia, and we were grateful for the positive support received. The merger would have been an exciting development, but no agreement acceptable to all parties could be reached.

Focus on the underlying business performance was sustained as a priority while the merger discussions were underway. The Group's continued strategic aim is to drive shareholder value through a combination of meeting our customers' requirements, further improvements in financial performance and enhanced competitive positions across the business. The focus of the Group's Strategic Actions in pursuit of these goals includes: growth in its cyber, intelligence and security businesses; addressing growth opportunities in electronic systems; driving further value from the Group's broad base of platforms and services positions; and increased business in international markets outside of the UK and US.

The evolution of BAE Systems has seen the Group's business develop from an equipment supply-centred model to one that now embraces a services culture. In 2012, 50% of the Group's sales were generated in services across a wide range of activities and geographies.

Services activities include in-service support in the UK for the Royal Air Force's trainer aircraft and fast jet fleets, and the Royal Navy's surface fleet. In Australia and Saudi Arabia, the Group provides a broadly-based range of support services to the armed forces.

BAE Systems provides extensive support to US armed forces through provision of land vehicle reset and upgrade programmes, rotary wing and other aircraft support, and naval ship repair services. The Group also manages complex facilities including ammunition production in the US and the UK.

BAE Systems' services activities also include the provision of extensive cyber and intelligence capabilities. The Group's strategy includes growing its positions in the cyber and intelligence services markets for governments, and pursuing organic growth opportunities in commercial cyber and security applications and systems.

Affordability is a key consideration for all the Group's customers and BAE Systems has been successful in reducing costs over a sustained period. Whilst necessary to address lower demand in some business areas, cost reduction has also been targeted to achieve competitive advantage. A regrettable but unavoidable element of these cost reduction measures is the impact on employment. Excluding M&A activity, net employee headcount (including contractors) reduced by approximately 3,600 during the year, bringing the total net reduction across the past four years to approximately 26,000. In addition, site rationalisation has continued. These efficiency improvements lead to benefits for customers as well as underpinning the Group's value proposition for shareholders.

US

BAE Systems' business in the US contributed approximately 40% of Group sales in 2012. The US business has felt the dual pressure of reduced activity in support of deployed operations in Iraq and Afghanistan, and measures to reduce US federal budget deficits. In particular, the US land vehicles business has, as forecast, seen significant year-on-year reductions from the peak of activity in 2008.

The US elections have introduced some additional defence procurement uncertainty with the administration entering a six-month period of Continuing Resolution from the end of September 2012.

Overhanging the US defence sector into 2013 is the potential impact of a sequestration or other budget reductions that could result in indiscriminate funding cuts. The Group bases its plans on conservative assumptions and continues to address its cost base accordingly.

PRELIMINARY RESULTS STATEMENT *(continued)*

UK
Defence budgets in the UK are expected to remain flat, but the recent stabilising of equipment and services requirements and the budget outlook has established a more predictable planning environment.

The Group's UK maritime business is experiencing a high level of activity. Growth is anticipated in the submarines business on the back of the multi-year Astute Class submarine programme and the build-up in engineering workload for the Successor programme. BAE Systems received further Successor funding during the year, with approximately 1,000 people now working on the programme.

Also in the UK maritime business, the last ship of the six-ship Type 45 destroyer programme completed sea trials. Good progress continues to be made on the Queen Elizabeth Class Carrier programme with delivery of major blocks underway for the assembly of the first of these two ships. Work continues on the design of the Type 26 ships to replace the UK's Type 23 frigates from early in the next decade. Type 26 production is expected to utilise a lower level of UK ship build capacity following the currently high levels on the Carrier programme. Discussions continue with the UK government to determine how best to sustain the capability to deliver complex warships in the UK in the future.

In the military air sector, European Tranche 2 Typhoon deliveries have continued and international prospects for Typhoon remain good with the potential to extend production into the next decade. The Group continues to deliver assemblies for the US-led F-35 Lightning II programme under Low-Rate Initial Production contracts.

International
In addition to its US and UK operations, BAE Systems continues to build on its positions in international markets. As well as established operations in Saudi Arabia, Australia and more recently India, the Group is pursuing multiple new business opportunities worldwide.

Defence remains a high priority in the Kingdom of Saudi Arabia. BAE Systems has a large involvement in the support of established Royal Saudi Air Force (RSAF) and Royal Saudi Navy programmes in the Kingdom.

Deliveries of RSAF Typhoon aircraft are contracted to recommence in 2013, following a contract amendment to enable UK final assembly of the balance of 48 aircraft under the original contract for 72.

Discussions to formalise Typhoon price escalation under the Salam programme remain ongoing.

Discussions have commenced on the next phase of support, following on from the three-year agreement that formed part of the arrangements for initial entry into service of the Typhoon aircraft.

Under the Saudi British Defence Co-operation Programme (SBDCP), orders totalling £3.4bn were awarded for support through to 2016, including the provision of manpower, logistics and training to the RSAF. In addition, a £1.6bn contract was awarded in May to support the RSAF's future aircrew training requirements involving the supply of, and initial support for, Hawk Advanced Jet Trainer and Pilatus training aircraft.

BAE Systems is the leading provider of equipment and support to the Australian armed forces. The Group's largest programme in Australia is the Canberra Class programme to build two 27,000 tonne Landing Helicopter Dock vessels for the Royal Australian Navy.

BAE Systems continues to develop its business in India. The Indian government has recently confirmed its intention to buy the M777 artillery system and negotiations for a third batch of 20 locally assembled Hawk aircraft are expected to commence in 2013.

In Oman, a £2.5bn contract for 12 Typhoon and eight Hawk aircraft and associated training and support has been awarded, and we are progressing opportunities for Typhoon in Malaysia and the United Arab Emirates.

In June, the business was awarded a $750m (£462m) CV90 combat vehicle contract in Norway.

Balance sheet and capital allocation

The Group recognises the importance to investors of a clear capital allocation policy, consistent with sustaining a strong investment grade credit rating, as part of its value proposition.

In addition to meeting its pension funding obligations, the Group expects to continue organic investment in its businesses to sustain and grow, plans to continue to pay dividends in line with its policy of a long-term sustainable cover of around two times underlying earnings[1] and to make accelerated returns of capital to shareholders when the balance sheet allows. Consistent with this approach, in February 2013, the Group initiated a three-year share repurchase programme of up to £1bn. Full implementation of this programme is subject to satisfactory resolution of Salam Typhoon price escalation negotiations. Discussions with the Group's UK pension scheme trustees have commenced to address any implications for deficit funding plans. Investment in value enhancing acquisitions will continue to be considered where market conditions are right, where they deliver on the Group's strategy and where they offer greater value than repurchasing the Group's own shares.

M&A activity

The Group's business portfolio is reviewed regularly to determine whether greater value can be created from the sale of a business rather than its retention, and three small business disposals were made during the year for a combined consideration of approximately £111m.

In March, the Group completed the sale of BAE Systems Safety Products Inc. and Schroth Safety Products GmbH (Safety Products). In July, the Safariland, LLC (Safariland) business and the assets comprising BAE Systems Tensylon High Performance Materials Inc. (Tensylon) were sold.

BAE Systems continues to seek bolt-on acquisitions that enhance routes to market or which provide rapid access to relevant technologies and capabilities.

In November, the Group agreed the acquisition of Marine Hydraulics International, Inc., a US marine repair, overhaul and conversion company, for cash consideration of approximately $69m (£42m). The acquisition is expected to complete in the first quarter of 2013.

Pension funding

Triennial funding valuations of the Group's two largest UK pension schemes, the BAE Systems Pension Scheme and the BAE Systems 2000 Pension Plan, were completed as at 31 March 2011. In 2012, agreement on revised deficit funding plans was reached with the trustees of those schemes and the next valuation will commence in April 2014.

Directors and management

In May, Michael Hartnall, a non-executive director, stood down from the Board having served nearly nine years in that capacity.

As previously announced, Sir Peter Mason stepped down as the Board's Senior Independent Director in January 2013. Nick Rose, a non-executive director, succeeds Sir Peter as the Board's Senior Independent Director. Sir Peter will step down from the Board at the Annual General Meeting in May 2013.

In June, Tom Arseneault was appointed Executive Vice President of the Product Sector businesses headquartered in the US and Chief Technology Officer for BAE Systems, Inc. Also in June, Lynn Minella was appointed Group Human Resources Director following the retirement of Alastair Imrie. On their appointment, both Tom and Lynn joined the Group's Executive Committee.

With effect from 30 March 2013, Larry Prior, Executive Vice President of the Service Sector businesses headquartered in the US and Chief Operating Officer for BAE Systems, Inc., and member of the Group's Executive Committee, will leave the Group to pursue other opportunities.

In February 2013, David Herr was appointed Executive Vice President of the Service Sector businesses and joined the Group's Executive Committee.

Dividend

The Board has recommended a final dividend of 11.7p per share making a total of 19.5p per share for the year, an increase of 4% over 2011. At this level, the annual dividend is covered 2.0 times by underlying earnings[1] (2011 2.1 times excluding the UK tax agreement benefit).

1 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).

PRELIMINARY RESULTS STATEMENT *(continued)*

Income statement – continuing operations

	2012 £m	2011 £m
Sales[1]	**17,834**	19,154
Underlying EBITA[2]	**1,895**	2,025
Return on sales	**10.6%**	10.6%
Profit/(loss) on disposal of businesses	**103**	(29)
Regulatory penalties	**–**	(49)
EBITA	**1,998**	1,947
Amortisation of intangible assets	**(226)**	(239)
Impairment of intangible assets	**(86)**	(109)
Finance costs[1]	**(275)**	(106)
Taxation expense[1]	**(337)**	(233)
Profit for the year	**1,074**	1,260

Exchange rates – average

	2012	2011
£/$	**1.585**	1.604
£/€	**1.233**	1.153
£/A$	**1.531**	1.553

Segmental analysis

	Sales[1]		Underlying EBITA[2]	
	2012 £m	2011 £m	2012 £m	2011 £m
Electronic Systems	**2,507**	2,645	**356**	386
Cyber & Intelligence	**1,402**	1,399	**124**	136
Platforms & Services (US)	**4,539**	5,305	**394**	478
Platforms & Services (UK)	**5,646**	6,258	**689**	658
Platforms & Services (International)	**4,071**	3,794	**417**	449
HQ	**267**	233	**(85)**	(82)
Intra-group	**(598)**	(480)	**–**	–
	17,834	19,154	**1,895**	2,025

The results of the Regional Aircraft line of business are shown within discontinued operations.

Sales[1] reduced by 7% reflecting lower volumes in the Land & Armaments business, and there being no contracted Typhoon aircraft deliveries in the year under the Salam Typhoon programme.

Underlying EBITA[2] Management uses an underlying profit measure to monitor the year-on-year profitability of the Group defined as earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.

Underlying EBITA[2] was £1,895m (2011 £2,025m) giving a return on sales of 10.6% (2011 10.6%).

Non-recurring items are defined as items that are relevant to an understanding of the Group's performance with reference to their materiality and nature. **Profit on disposal of businesses** of £103m in 2012 includes the disposals of Safety Products and Safariland, and assets comprising the Tensylon business, which were part of the Land & Armaments business. The loss of £29m in 2011 arose on the disposals of the Advanced Ceramics and Swiss-Photonics businesses.

Amortisation of intangible assets is £13m lower at £226m mainly reflecting the completion of deliveries under the Family of Medium Tactical Vehicles (FMTV) contract in 2011.

Impairment of intangible assets, including goodwill, of £86m mainly relates to the Safariland and Tensylon businesses sold in July 2012, and the Commercial Armored Vehicles business expected to be sold in the first quarter of 2013. In 2011, charges included those taken against the Safety Products (£66m) and Naval Ships (£34m) businesses.

Finance costs[1] were £275m (2011 £106m). The underlying interest charge, which excludes pension accounting, marked-to-market revaluation of financial instruments and foreign currency movements, was £204m. In the prior year, the underlying interest charge of £199m included £28m relating to the early redemption of debt in connection with the disposal of the Regional Aircraft Asset Management business. Costs in 2012 include interest on the £400m debt refinancing completed in June and a higher level of net present value charges on long-term liabilities.

Taxation expense[1] reflects an effective tax rate of 25%. In 2011, excluding the benefit of an agreement with the UK tax authorities addressing a number of items, including research and development tax credits, the effective tax rate was 26%. The calculation of the effective tax rate is shown below:

Calculation of the effective tax rate

	2012 £m	2011 £m
Profit before taxation	**1,411**	1,493
(Deduct)/add back:		
(Profit)/loss on disposal of businesses	**(103)**	29
Regulatory penalties	**–**	49
Goodwill impairment	**57**	94
	1,365	1,665
Taxation expense[1] (excluding 2011 UK tax agreement)	**337**	430
UK tax agreement	**–**	(197)
Taxation expense[1]	**337**	233
Effective tax rate	**25%**	14%
Effective tax rate (excluding 2011 UK tax agreement)	**25%**	26%

The underlying tax rate for 2013 is expected to be between 23% and 25%, with the final number dependent on the geographical mix of profits.

Earnings per share – continuing operations

Underlying earnings[3] per share was 38.9p, a decrease of 2% on 2011 (excluding the UK tax agreement benefit).

Basic earnings per share, in accordance with International Accounting Standard (IAS) 33, Earnings per Share, was 32.8p compared with 37.0p in 2011 (including the UK tax agreement benefit).

Cash flow

Reconciliation of cash inflow from operating activities[4] to net cash/(debt) (as defined by the Group)

	2012 £m	2011 £m
Cash inflow from operating activities[4]	**2,916**	951
Capital expenditure (net) and financial investment	**(293)**	(268)
Dividends received from equity accounted investments	**94**	88
Assets contributed to Trust	**(25)**	(137)
Operating business cash flow	**2,692**	634
Interest	**(147)**	(180)
Income from financial assets at fair value through profit or loss	**–**	4
Taxation	**(115)**	(257)
Free cash flow	**2,430**	201
Acquisitions and disposals	**96**	(256)
Purchase of equity shares (net)	**(16)**	(509)
Equity dividends paid	**(620)**	(606)
Dividends paid to non-controlling interests	**(11)**	(22)
Cash outflow from matured derivative financial instruments	**(119)**	(34)
Movement in cash collateral	**(2)**	–
Movement in cash received on customers' account[5]	**1**	13
Foreign exchange translation	**92**	(20)
Other non-cash movements	**(25)**	36
Total cash inflow/(outflow)	**1,826**	(1,197)
Opening net debt (as defined by the Group)	**(1,439)**	(242)
Closing net cash/(debt) (as defined by the Group)	**387**	(1,439)

Components of net cash/(debt) (as defined by the Group)

	2012 £m	2011 £m
Debt-related derivative financial assets	**22**	56
Cash and cash equivalents	**3,355**	2,141
Loans – non-current	**(2,967)**	(2,682)
Loans and overdrafts – current	**(21)**	(518)
Less: Cash received on customers' account[5]	**(2)**	(3)
Less: Assets held in Trust	**–**	(403)
Less: Cash held for charitable contribution to Tanzania	**–**	(30)
Net cash/(debt) (as defined by the Group)	**387**	(1,439)

Operating business cash flow

	2012 £m	2011 £m
Electronic Systems	**256**	268
Cyber & Intelligence	**113**	123
Platforms & Services (US)	**314**	410
Platforms & Services (UK)	**1,719**	69
Platforms & Services (International)	**506**	80
HQ	**(214)**	(308)
Discontinued operations	**(2)**	(8)
Operating business cash flow	**2,692**	634

Cash inflow from operating activities[4] was £2,916m (2011 £951m), which includes down-payments received on new contracts to Saudi Arabia and Oman, and contributions in excess of service costs for the UK and US pension schemes totalling £507m (2011 £375m).

The outflow from **net capital expenditure and financial investment** of £293m (2011 £268m) was only marginally higher than 2011.

Dividends received from equity accounted investments, primarily MBDA, Advanced Electronics Company, FNSS and Eurofighter, totalled £94m (2011 £88m). This excludes a £424m non-cash special dividend received from MBDA during the year.

Assets contributed to Trust comprise £25m of payments made into Trust for the benefit of the BAE Systems 2000 Pension Plan. In 2011, £137m was paid into Trust for the benefit of the Group's main pension scheme.

Taxation payments were £142m lower at £115m primarily reflecting tax refunds following the 2011 UK tax settlement and timing differences on UK and US tax payments, and reflect the level of pension deficit funding to the UK schemes.

Net cash inflow in respect of **acquisitions and disposals** of £96m mainly comprises the disposals of Safety Products and Safariland, and assets comprising the Tensylon business. The prior year outflow of £256m mainly comprised the acquisition of L-1 Identity Solutions, Inc.'s Intelligence Services Group, Norkom Group plc, ETI A/S, Fairchild Imaging, Inc. and stratsec.net Pty Limited (£524m), less the net proceeds from the disposal of the Regional Aircraft Asset Management business (£98m) and the Group's residual shareholding in Saab AB (£152m).

The **net purchase of equity shares** of £509m in the prior year included 184 million shares purchased under the buyback programme at a cost of £500m (excluding transaction costs of £3m).

As a consequence of movements in US dollar and Euro exchange rates during the year, there has been a **cash outflow from matured derivative financial instruments** of £119m (2011 £34m) from rolling hedges on balances with the Group's subsidiaries and equity accounted investments.

Foreign exchange translation primarily arises in respect of the Group's US dollar-denominated borrowing.

Net cash (as defined by the Group) is £387m, a net inflow from the net debt position of £1,439m at the start of the year. Cash and cash equivalents of £3,355m (2011 £2,141m) are held primarily for pension deficit funding, payment of the 2012 final dividend, the share repurchase programme and management of working capital.

In June 2012, the Group issued a £400m, ten-year bond with an annual coupon of 4.125% intended for general corporate purposes, including the repayment of debt securities at maturity in 2014.

1 Including share of equity accounted investments.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).
4 Excludes the £428m contribution from Trust to the UK pension schemes and the £29.5m charitable contribution for the benefit of the people of Tanzania in connection with the global settlement with the UK's Serious Fraud Office in 2010, both made in 2012, as the amounts had been deducted from the Group's net cash/(debt).
5 Cash received on customers' account is the unexpended cash received from customers in advance of delivery which is subject to advance payment guarantees unrelated to Group performance. It is included within trade and other payables in the consolidated balance sheet.

REPORTING SEGMENTS: ELECTRONIC SYSTEMS

Electronic Systems, with 13,000 employees[1], comprises the US and UK-based electronics activities, including electronic warfare systems and electro-optical sensors, military and commercial digital engine and flight controls, next-generation military communications systems and data links, persistent surveillance capabilities, and hybrid electric drive systems.

Operational key points

- Sustained a leadership position in the airborne electronic warfare market
- Strengthened position in high growth commercial aircraft electronics market
- Won key development contracts in the classified area
- Continued focus on increasing productivity and efficiency
- Business recovery complete following disruption from flood damage at the Johnson City facility
- £0.2bn of research and development expenditure[5] in 2012

Financial key points

- Underlying order backlog[1,4] increased in challenging business environment
- Sales[1] reduction from operational tempo-driven activity on Thermal Weapon Sights
- Return on sales of 14.2%
- Cash flow[3] conversion of underlying EBITA[2] at 95%, before pension deficit funding

	2012	2011	2010
Funded order intake[1]	**£2,540m**	£2,620m	£2,894m
Order backlog[1,4]	**£3.6bn**	£3.6bn	£3.5bn
Sales[1]	**£2,507m**	£2,645m	£2,969m
Underlying EBITA[2]	**£356m**	£386m	£455m
Return on sales	**14.2%**	14.6%	15.3%
Cash inflow[3]	**£256m**	£268m	£367m

Financial performance

Order backlog[1,4], excluding the impact of US dollar exchange translation, increased despite the impact of contracting delays as the US administration operated federal budgets under Continuing Resolution limitations.

On a like-for-like basis, sales[1] reduced by 7% on 2011 primarily reflecting the completion of deliveries of Thermal Weapon Sights as operational tempo-driven activity reduces. Sales in the Commercial Aircraft electronics business increased by 11%.

Underlying EBITA[2] was £356m (2011 £386m). Return on sales was 14.2% (2011 14.6%).

Cash flow[3] conversion of underlying EBITA[2] was 95%, before pension deficit funding.

Operational performance

Following severe flooding in September 2011, operations formerly conducted at the Electronic Systems facility in Johnson City, New York, have been moved to Endicott, New York. After a year of recovery efforts, operational capability has been restored and programmes are back on schedule.

Electronic Combat The business maintains its leadership position in the electronic warfare market, with continued focus on the F-35 Lightning II Systems Design and Development programme, planning for the flight test programme starting in 2013. The business progressed Low-Rate Initial Production (LRIP) Lot 5 and 6 deliveries during the year, and has responded to the LRIP Lot 7 request for proposal, which includes production aircraft for international customers.

In support of the US Navy's Next-Generation Jammer, which will replace the ageing jammer currently on certain US Navy aircraft, a $20m (£12m) modification was received to expand the scope of the existing technology maturation contract. BAE Systems is one of three bidders on the next phase technology development contract valued at approximately $300m (£185m).

The Digital Electronic Warfare System (DEWS) continues to secure new contract awards, including a six-year, $0.4bn (£0.2bn) contract to upgrade 70 F-15 aircraft for the Royal Saudi Air Force. Initial flight testing providing advanced radar warning and countermeasure capabilities is scheduled to begin in March 2013. The business continues to pursue other export opportunities for the DEWS suite.

Also in international markets, the business received three contracts totalling $86m (£53m) to provide F-16 support equipment, test systems and spares to the governments of Oman, Indonesia and Iraq for delivery by early 2014.

Survivability & Targeting In early 2012, the US Army awarded the business a two-year, $38m (£23m) contract to develop the Common Infrared Countermeasures capability. Using its Boldstroke® system, an integrated aircraft survivability system for protecting aircraft from infrared-guided missiles and other threats, the business will provide increased system capability in a smaller, more energy efficient package. Following a competitor protest, the award was upheld by the US Government Accountability Office and work restarted in June. Initial test systems are in progress, with the first units scheduled for government acceptance ahead of schedule.

1 Including share of equity accounted investments.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 6).
3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.
4 Comprises funded and unfunded unexecuted customer orders.
5 Includes both Group-funded and customer-funded expenditure.

The Advanced Precision Kill Weapon System programme passed tests on several airborne platforms. With deployment in theatre and positive performance feedback, the US Navy has authorised Full-Rate Production of the system and awarded a base contract valued at $28m (£17m) for 985 units and a Full-Rate Production option of $41m (£25m) for 1,476 units.

Under a $37m (£23m) subcontract, BAE Systems continues to support the engineering and manufacturing development of the Joint and Allied Threat Awareness System, a next-generation warning system to enhance aircraft survivability for the US Navy.

The Thermal High-Altitude Area Defence seeker programme provides a transportable, rapidly deployable, ground-based capability to intercept and destroy ballistic missiles inside or outside the atmosphere during their final phase of flight. BAE Systems has received an initial amount of $87m (£54m) in combined US government and Foreign Military Sales to the United Arab Emirates on the programme, including a base quantity of 146 seekers with an option for up to a further 147.

Deliveries of Thermal Weapon Sights to the US Army in support of military operations in Iraq and Afghanistan were completed.

BAE Systems has responded to a US Army request for proposal for its Joint Effects Targeting System programme, which has been designed to enhance dismounted, forward-deployed soldiers' ability to accurately locate positions and target precision-guided munitions fire support. An award decision is expected in the first half of 2013 for a 26-month Engineering and Manufacturing Development phase, which will be followed by a Low-Rate Initial Production award competition.

Communications & Control The F-35 Lightning II programme continues to be a key platform for the Group's avionics products. Deliveries continue on plan for the active inceptor system out of Rochester, UK, and the vehicle management system out of Endicott, New York. The business has continued to pursue additional opportunities expanding its content on the platform.

Leveraging commercial technology to create a low size, weight and power design, the business launched the PHOENIX™ family of networking radios to integrate easily into US Army ground combat vehicles. In October, the business responded to the US Army's next-generation Mid-tier Networking Vehicular Radio request for proposal with its two-channel PHOENIX-SC radio, with an award decision expected in 2013.

Intelligence, Surveillance & Reconnaissance (ISR) The business continues to provide Wide Area Airborne Surveillance capability for the US Air Force and US Army. These key programmes are based on two wide-area, high-resolution imaging sensor systems, the Airborne Wide Area Persistent Surveillance System, which has been operational for over 12,000 hours in theatre, and the Autonomous Real-time Ground Ubiquitous Surveillance – Imaging System. These systems enable observation of very wide areas of interest with sufficient imagery resolution to meet intelligence and surveillance needs.

The business is providing state-of-the-art processing capabilities to Boeing for the US Navy's P8A Poseidon programme. The mission computer suite has robust, flexible and rugged open architecture providing high performance in the military environment. Over 30 initial systems have been delivered and a contract for Full-Rate Production Lot 1 has been awarded.

As a leader in the Identification Friend or Foe market, the business has a strong order backlog[4] driven by the Mode 5 cryptographic system upgrades, which have been incorporated into products deployed on multiple US Department of Defense platforms. Production has begun and is expected to continue to the end of the decade.

Commercial Aircraft electronics The business continues to be well positioned for growth in worldwide demand for commercial aviation through its engine and flight controls activities.

FADEC Alliance, a new joint venture between FADEC International (a joint venture between BAE Systems and Sagem) and GE Aviation, began development of the Full-Authority Digital Engine Controls for CFM International's LEAP and GE Aviation's Passport family of engines.

Ongoing development of the primary flight control electronics and active side sticks for Embraer's KC-390 military transport aircraft is raising the Group's profile in the emerging Brazilian aerospace industry. The first flight of the KC-390 is expected in 2014.

HybriDrive® propulsion BAE Systems has delivered 3,800 hybrid diesel-electric propulsion systems since 2004, which are now in service with over 60 operators.

In April 2012, European bus manufacturer, Iveco Irisbus, announced that it had been awarded Europe's largest single order for 132 diesel-electric hybrid buses for Dijon and Bordeaux in France. Prior to this award, Iveco Irisbus had delivered approximately 20 diesel-electric hybrid buses equipped with BAE Systems' propulsion systems.

The business has progressed solutions for battery reliability issues in the field from its first generation lithium-ion battery packs. In addition, ownership of the current battery supplier has changed and the business is working with the new owner to minimise the impact on the Group and its customers.

Looking forward

Efforts to reduce the US government's budget deficit are likely to impact all areas of government spend. A Continuing Resolution on the 2013 fiscal budget has been passed through to March 2013 and the risk of further reductions in US defence budgets remains, including the impact of sequestration.

Whilst likely funding reductions and the resultant slow down or cancellation of ongoing and new programmes could impact the business, Electronic Systems remains well positioned with a balanced portfolio that will enable it to respond to changing US Department of Defense priorities whilst maintaining its emphasis on cost reduction. The business expects to benefit from its incumbent positions on core platforms, and from positions in areas such as commercial aircraft electronics and international defence programmes.

REPORTING SEGMENTS: CYBER & INTELLIGENCE

Cyber & Intelligence, with 8,200 employees[1], comprises the US-based Intelligence & Security business and UK-headquartered BAE Systems Detica business, and covers the Group's cyber, secure government, and commercial and financial security activities.

Operational key points

- The US-based business continues to perform well on existing programmes and secured strategic contract awards with existing customers
- The US-based business continues to invest in differentiating technologies, such as activity-based intelligence and cybersecurity, including a leading edge network operations and security centre environment, to support a pipeline of submitted bids of $2.9bn (£1.8bn) at the end of 2012
- BAE Systems Detica continues to invest in products and capability, including its Security Operations Centre
- BAE Systems Detica awarded a contract by Vodafone for next-generation enterprise secure networks for mobile devices

Financial key points

- Funded order intake[1] and sales[1] were broadly unchanged from 2011
- Return on sales impacted by investment in the BAE Systems Detica business for future growth
- Cash flow[3] conversion of underlying EBITA[2] at 91%

	2012	2011	2010
Funded order intake[1]	**£1,454m**	£1,443m	£1,300m
Order backlog[1,4]	**£1.0bn**	£1.1bn	£0.9bn
Sales[1]	**£1,402m**	£1,399m	£1,201m
Underlying EBITA[2]	**£124m**	£136m	£108m
Return on sales	**8.8%**	9.7%	9.0%
Cash inflow[3]	**£113m**	£123m	£89m

Financial performance

Funded order intake[1] and sales[1] were broadly unchanged from 2011.

Order backlog[1,4] reduced to £1.0bn (2011 £1.1bn). There is a significant number and value of competitive bids in the Intelligence & Security business awaiting award decisions.

Underlying EBITA[2] was £124m (2011 £136m). Return on sales reduced to 8.8% (2011 9.7%) reflecting increased levels of investment in the BAE Systems Detica business in support of targeted future growth in commercial and international markets.

Operating cash inflow[3] was £113m (2011 £123m), which represents a conversion of underlying EBITA[2] of 91%.

Operational performance

Intelligence & Security

The US-based Intelligence & Security business delivers a broad range of services, including secure IT solutions, cybersecurity, geospatial solutions and intelligence analysis to enable the US military and government to recognise, manage and defeat threats. The business is structured into four key business areas that provide specific domain expertise, whilst working closely together to provide enterprise-wide support to a range of customers, and key agencies in the intelligence, defence, homeland security and civilian markets.

Information Technology & Cybersecurity Solutions develops, deploys and maintains mission applications focused on information sharing, knowledge management and enhanced enterprise mission IT solutions for the US federal, civilian and defence intelligence communities. The business also provides analytics, cyber analysis and real-time network forensics.

Through 2012, work continued on the Solutions for the Information Technology Enterprise Indefinite Delivery, Indefinite Quantity (IDIQ) contract, with the business as the prime contractor, receiving task orders now worth a total of $344m (£212m). Since the project began, approximately 700 security-cleared IT experts, deployed across 84 locations in 14 countries, have assisted the US Defense Intelligence Agency in delivering IT services to 50,000 Department of Defense personnel by standardising global IT operations and reducing the time taken to deliver technician services.

Continuing work on the Next-Generation Desktop Environment (NGDE) programme for the US Defense Intelligence Agency, the business has virtualised hundreds of applications and deployed data centre infrastructure to 13 sites, now supporting over 12,000 global analyst workstations. The NGDE is an enterprise networking environment based on virtual desktop infrastructure.

The Security Operations Centre in the US protects the Group's networks by monitoring its global intranet, with more than 100,000 network interfaces serving employees across five home markets and offices in over 100 countries. Services include security engineering, risk analysis, support of IT hardware and software, IT engineering and applications, and global enterprise monitoring and security incident response.

GEOINT-ISR (Geospatial Intelligence – Intelligence, Surveillance and Reconnaissance) develops and supports software systems and mission applications for geospatial tasking, including data collection, processing, exploitation and dissemination, as well as mission planning, Intelligence, Surveillance and Reconnaissance (ISR), precision targeting, and command and control for the US defence and intelligence communities.

1 Including share of equity accounted investments.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 6).
3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.
4 Comprises funded and unfunded unexecuted customer orders.

The business was awarded a five-year, $106m (£65m) contract by the National Geospatial-Intelligence Agency (NGA), under which engineers will design, develop and implement a transformational solution enabling the US government to evolve from its current image library to a standardised image storage, management and dissemination process. This is an important strategic win that will drive future GEOINT and imagery systems development.

In December 2012, BAE Systems was awarded a multi-year, $60m (£37m) contract to provide activity-based intelligence systems, tools and support for mission priorities for the NGA. This award is a task order under the NGA's Total Application Services for Enterprise Requirements programme, a five-year IDIQ contract.

Global Analysis provides mission-enabling analytic solutions and support to operations across the US homeland security, law enforcement, defence, intelligence and counterintelligence communities.

The business continues to provide approximately 450 security cleared analysts working alongside forward deployed US defence personnel as part of the Counter Improvised Explosive Device (C-IED) programme, with a total value of funded orders of approximately $450m (£277m) over the two years of the contract. The business is now working with the customer to manage staffing levels in line with reducing mission requirements.

The business is executing well on the Full Motion Video and Geospatial Imagery Analysis contract awarded in 2011, with a contract value of $402m (£248m) and over 400 employees being utilised.

SpecTal provides US government customers with specialised security and intelligence mission support, including intelligence analysis, targeting operations support, training and IT deployment.

With the 2011 acquisition of L-1 Identity Solutions' Intelligence Services Group, a key contract with an intelligence community customer was gained. The contract has since been re-competed and SpecTal was part of the winning bid team serving as a major subcontractor on the five-year programme.

BAE Systems Detica

BAE Systems Detica continues to build a business that provides security and intelligence products and services to both government and commercial customers. In July, the stratsec business in Australia, acquired in 2011, and a new security entity in India were integrated into BAE Systems Detica. The business is also focused on developing opportunities in the Americas' commercial market.

Cyber Security Demand is growing across both government and commercial sectors, with contracts secured with a global law firm and a US financial institution in 2012. The Security Operations Centre became fully operational in 2012, providing services to detect and remediate advanced cyber attacks for clients.

The business was one of four companies selected by the UK's Government Communications Headquarters (GCHQ) to work in partnership on a new Cyber Incident Response pilot programme, a government quality-assured service that organisations can turn to when they have suffered a cybersecurity incident.

Detica NetReveal® As a provider of risk, fraud and compliance solutions to the global financial services industry, orders of £74m were received during the year, including contracts in new business areas of healthcare and insurance in the US.

Global Communications Solutions is a provider of specialist communications equipment, including monitoring and lawful intercept solutions, for use by government and commercial clients.

During 2012, a review of routes-to-market was carried out, resulting in necessary changes which adversely impacted the 2012 financial performance of the business.

Services The business, which provides consultancy, systems integration and managed services, was impacted by challenging market conditions in both the UK government and commercial sectors.

Orders in the year included a contract under a business change programme for a complex UK cross-government programme and a managed services contract with Vodafone for the provision of next-generation enterprise secure networks for mobile devices. The business was unsuccessful in its bid to provide services under the UK government's Disclosure and Barring Service.

The business continues to develop opportunities internationally, in both the Middle East and, with the addition of stratsec, the Asia Pacific region.

Looking forward

Efforts to reduce the US government's budget deficit are likely to impact all areas of government spend. A Continuing Resolution on the 2013 fiscal budget has been passed through to March 2013 and the risk of further reductions in US defence budgets remains, including the impact of sequestration.

Growth opportunities remain, particularly in critical, mission-focused areas, such as next-generation ISR, Multi-INT fusion (the seamless synthesis of the individual intelligence disciplines to enable more complete situational awareness), counter intelligence and enterprise solutions for big data problems.

The US market is experiencing delays in procurement awards and descoping of existing contracts as US government agencies look to reduce IT budgets. Sales in 2013 are expected to be impacted by the completion of the C-IED contract as the US withdraws from Afghanistan. However, the business expects an enduring need to provide data management solutions, including the rapid collection, processing and dissemination of data to intelligence community customers and the US military. The business is well prepared to compete in this price-sensitive market through its customer intimacy, innovation and continued cost management.

BAE Systems Detica expects growth in cyber and intelligence, both in the UK and overseas government markets, with increasing demand for products and services in commercial markets to manage cyber threats, counter financial fraud and improve compliance, including next-generation security for mobile devices.

REPORTING SEGMENTS: PLATFORMS & SERVICES (US)

Platforms & Services (US), with 21,300 employees[1], comprises the US-headquartered Land & Armaments business, with operations in the US, UK, Sweden and South Africa, together with US-based services and sustainment activities, including ship repair and munitions services.

Operational key points

- Growth in US ship repair activities
- Executing munitions infrastructure and facility operations management contracts
- Strategic international win with Korean F-16 upgrade down-select
- Continued to protect Bradley franchise with $376m (£231m) in related awards
- Awarded a $750m (£462m) contract for CV90 armoured combat vehicles to Norway
- Letter of Request received from Indian government for 145 M777 howitzers
- Continued consolidation in the Land & Armaments business
- Business disposals of Safety Products, Safariland and Tensylon completed

Financial key points

- Sales[1] reduced by 2% in Support Solutions business and by 23% in Land & Armaments business
- Return on sales increased to 8.8% in Support Solutions business and reduced to 8.6% in Land & Armaments business
- Support business delivered an increase in order backlog[1,4] and strong operating cash flow[3]

	2012	2011	2010
Funded order intake[1]	**£5,010m**	£5,077m	£5,605m
Order backlog[1,4]	**£8.4bn**	£8.7bn	£9.1bn
Sales[1]	**£4,539m**	£5,305m	£7,671m
Underlying EBITA[2]	**£394m**	£478m	£728m
Return on sales	**8.7%**	9.0%	9.5%
Cash inflow[3]	**£314m**	£410m	£967m

Financial performance

Sales[1] were £4.5bn (2011 £5.3bn), representing a like-for-like reduction of 13%. Sales[1] at Support Solutions were just 2% below 2011. Like-for-like sales[1] at Land & Armaments reduced by 20% primarily reflecting the completed Family of Medium Tactical Vehicles programme, and lower volumes on Bradley, Caiman and Mine Resistant Ambush Protected vehicles.

Underlying EBITA[2] was £394m (2011 £478m). Return on sales reduced to 8.7% (2011 9.0%). Return on sales at Support Solutions increased from 7.5% to 8.8% benefiting from certain legal settlements. Return on sales at Land & Armaments reduced from 9.9% to 8.6% reflecting accelerated rationalisation charges in respect of the Newcastle vehicle manufacturing site in the UK and certain legal claims.

Operating cash inflow[3] reduced to £314m (2011 £410m) reflecting continued investment in the UK munitions facilities in the Land & Armaments business. Excluding pension deficit funding, cash flow[3] conversion of underlying EBITA[2] at Support Solutions and Land & Armaments was 100% and 83%, respectively.

Operational performance

Support Solutions

The US-based ship repair business achieved 2012 commitments under its Multi-Ship, Multi-Option contract vehicles with the US Navy, receiving superior scores on award fee assessments. The business was awarded new commercial maritime construction contracts totalling $190m (£117m), including four platform supply vessels and two barges.

In the complex infrastructure services market, the business secured the Holston Army Ammunition Plant award of a follow-on five-year, $145m (£89m) contract for facility operations. In addition, the business completed the planned transition to begin operating the Radford Army Ammunition Plant on 1 July 2012 under a contract worth approximately $850m (£523m) over ten years. In October 2012, the business was notified that it had not been awarded the Lake City Army Ammunition Plant management contract.

The business won a five-year, $44m (£27m) Navy Munitions Command – Hawaii contract to handle and store munitions, which continues more than 27 years of distinguished service recognised by the US Navy.

The US Naval Air Warfare Center Aircraft Division awarded a follow-on five-year, $193m (£119m) contract to provide Command, Control, Communications, Computers and Intelligence (C4I), lifecycle support, integration and test engineering, and technical services, supporting a broad range of air, land and sea platforms.

The business was awarded a $60m (£37m) task order under the US Department of Defense's Joint Improvised Explosive Device Defeat Organization contract to develop and implement a five-year training programme.

Support Solutions continues to pursue international aircraft upgrade and modification opportunities. In August, the Republic of Korea selected BAE Systems to upgrade avionics and electronic systems on its fleet of more than 130 F-16 aircraft. The programme is expected to be contracted in 2013 and is forecast to be worth over $500m (£308m) over ten years.

In November, the business was awarded a contract by the US Navy for depot level maintenance and logistics support for more than 360 T-34/T-44/T-6 training aircraft. If all options are exercised, the contract would be valued at more than $400m (£246m) over five years.

BAE Systems is pursuing a potential bid as prime contractor for the US Air Force's T-X programme to replace the T-38 jet training

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4 Comprises funded and unfunded unexecuted customer orders.

system with its Hawk trainer aircraft. The programme is valued at between $11bn (£7bn) and $17bn (£10bn). The US Air Force is expected to announce the timing of its request for proposals in 2013.

In the Protection Systems business, contracts have been secured totalling over $200m (£123m) for the supply of Enhanced Small Arms Protective Inserts, Tactical Vests and Modular Lightweight Load Carrying Equipment.

In November, the Group announced a definitive agreement to acquire Marine Hydraulics International, Inc., a marine repair, overhaul and conversion company with shipyard, pier and waterfront facilities in Norfolk, Virginia. The proposed acquisition, which is expected to complete during the first quarter of 2013, complements the existing ship repair business.

Land & Armaments

During 2012, Land & Armaments completed the disposals of its Safety Products, Safariland and Tensylon businesses. The disposal of the Commercial Armored Vehicles business is expected to complete in the first quarter of 2013. In September, the business announced that production of military equipment at its Fairfield, Ohio, facility would be moved to Sealy, Texas, in early 2013. The Protection Systems business, formerly reported in Land & Armaments, was transferred to Support Solutions at the start of the year. Management of the Combat Vehicles (UK) business was transferred to Platforms & Services (UK) from 1 October 2012.

Vehicle Systems This division comprises the franchises in tracked and wheeled vehicles.

The business received a $306m (£188m) contract modification in August to upgrade 353 Bradley fighting vehicles, extending Bradley activity into 2014. This production contract is in addition to $70m (£43m) to purchase upgrade materials for the Bradley programme.

The business has received the Paladin Integrated Management (PIM) Low-Rate Initial Production request for proposal scheduled for submission in early 2013. Testing continues on the contracted prototypes activity. An award decision is expected in 2013.

On the Ground Combat Vehicle (GCV) programme, the business continues test work under the $450m (£277m) technology development phase. Continuing development testing demonstrates that the technology provides more power, efficiency and vehicle performance than comparable conventional drive systems.

In January 2012, the business was awarded a £65m contract to supply 48 BvS10 armoured all-terrain vehicles and associated support to Sweden. The business was also awarded a £38m contract to regenerate the British Royal Marines' fleet of BvS10 vehicles. The last of 53 BvS10s ordered by France was delivered by year end.

In June, the business was awarded a $750m (£462m) contract to upgrade Norway's existing 103-vehicle CV90 fleet and build new vehicle chassis to deliver 144 CV90s in five different configurations, including a variant equipped with a sensor suite for improved surveillance capability.

All deliveries of the Caiman Multi-Terrain Vehicle were delivered to contract schedule, with re-fit and integration of 592 vehicles completed at the Mine Resistant Ambush Protected (MRAP) sustainment facility in November.

In August, the business was selected as part of the industry team led by Lockheed Martin for the engineering and manufacturing development phase of the US government's potentially large Joint Light Tactical Vehicle programme.

The South African business continues to execute on a £39m contract for 73 RG31 Mobile Mortar Platforms for the United Arab Emirates and a £43m order for 110 RG32 patrol vehicles for the Swedish Defence Force that were secured in December 2011.

The business secured places on all the amphibious trade studies, demonstrators and hull survivability demonstrations, allowing the US Marine Corps customer to evaluate design concepts based on a new design or an upgrade to current vehicles.

In November, Denmark announced that eight bids had been received in response to its requirement for up to 450 armoured vehicles. BAE Systems bid a version of the CV90, which Denmark already operates. The award decision is expected in late 2013.

In Canada, following a one-year delay, a new request for proposal was released for up to 138 Close Combat Vehicles. BAE Systems submitted a proposal based on its CV90 armoured combat vehicle.

The business was unsuccessful in its bid for the Tactical Armoured Patrol Vehicle programme for the Canadian armed forces.

Weapons Systems & Support This division comprises munitions and artillery activities.

In naval armaments, orders for six Mk110 57mm naval guns were received for the US Coast Guard and to equip the US Navy's Littoral Combat Ships.

During the year, Australia announced its intention to buy 19 M777 howitzers to augment the 35 it already operates. In addition, the Indian government has issued a Letter of Request to the US government under the US Foreign Military Sales process for the supply of 145 M777 howitzers for the Indian Army.

Under the 15-year Munitions Acquisition Supply Solution contract, the UK Ministry of Defence placed an order to meet its 2015 munitions requirement reflecting lower demand and quantities deferred from previous years. This anticipated lower volume results from armed force cuts and the draw-down of Afghanistan operations. Efficiencies achieved through a £123m transformation of UK munitions manufacturing facilities and support from the UK Ministry of Defence position the business to offset this reduction with exports.

Joint Ventures FNSS, BAE Systems' Turkish joint venture, continues to produce and upgrade tracked and wheeled military vehicles for international customers. Design work and successful mine testing were completed on a $559m (£344m) programme to produce 259 8x8 wheeled armoured vehicles in 12 different variants for the Malaysian Army. Production has commenced and the first Infantry Fighting Vehicles are scheduled to be delivered in 2013.

Looking forward

Efforts to reduce the US government's budget deficit are likely to impact all areas of government spend. A Continuing Resolution on the 2013 fiscal budget has been passed through to March 2013 and the risk of further reductions in US defence budgets remains, including the impact of sequestration.

In February 2013, the Group was notified that the US Navy was considering the potential to cancel, defer or de-scope 13 ship availability contracts, resulting in the decision to issue conditional Worker Adjustment and Retraining Notification (WARN) Act notices to nearly 3,600 employees in the ship repair business.

Whilst downward pressure will be seen across the services market as a whole, potential cancellations and delays in new programmes may present opportunities to sustain and modernise existing platforms.

In the near term, Land & Armaments continues to operate in a challenging market environment. To offset these pressures and remain viable in the future, the business is investing to protect current programme positions like Bradley modernisation and UK munitions, establish new US domestic programmes such as PIM and GCV, and to win export programmes. The business continues to drive rationalisation efforts, efficiencies and cost reduction in order to remain competitive.

REPORTING SEGMENTS: PLATFORMS & SERVICES (UK)

Platforms & Services (UK), with 27,900 employees[1], comprises the Group's UK-based air, maritime and combat vehicle activities, and certain shared services activities.

Operational key points

– 46 Typhoon Tranche 2 aircraft delivered to the partner nations

– £2.5bn Typhoon and Hawk contract for Oman secured

– £446m contract awarded for European support on Typhoon

– First F-35 Lightning II aircraft accepted by the UK Ministry of Defence (MoD)

– Fifth Type 45 destroyer accepted off-contract and support provided for all Royal Navy Type 45 deployments

– Settlement reached with the Government of the Republic of Trinidad and Tobago in respect of the cancelled Offshore Patrol Vessels (OPV) programme

– Two OPVs delivered to the Brazilian Navy

– £0.8bn of customer funding received for ongoing design and development of the Successor submarine, and continuing production of the fourth Astute Class submarine

– £0.7bn of research and development expenditure[5] in 2012

Financial key points

– Order backlog[1] increased by £2.5bn on significant awards for Oman Typhoon and Hawk and Saudi training aircraft

– 10% decrease in sales[1] pending recommencement of Salam Typhoon deliveries in 2013

– Return on sales improved to 12.2%

– Strong cash flow[3] performance on significant contract advances

	2012	2011	2010
Funded order intake[1]	**£8,077m**	£4,355m	£3,968m
Order backlog[1]	**£21.2bn**	£18.7bn	£21.0bn
Sales[1]	**£5,646m**	£6,258m	£6,529m
Underlying EBITA[2]	**£689m**	£658m	£522m
Return on sales	**12.2%**	10.5%	8.0%
Cash inflow[3]	**£1,719m**	£69m	£191m

Financial performance

Funded order intake[1] in the year increased to £8.1bn following the award of significant contracts for the supply of 12 Typhoon and eight Hawk aircraft to Oman (£2.5bn), and for training aircraft for the Royal Saudi Air Force (£1.6bn).

Sales[1] in 2012 were £5.6bn, 10% lower than 2011, reflecting no contractual aircraft deliveries on the Salam Typhoon programme in 2012 and the completion of South African Gripen aircraft deliveries in 2011.

Underlying EBITA[2] was £689m (2011 £658m). Return on sales increased to 12.2% benefiting from strong programme execution, particularly on the European Typhoon and Type 45 programmes.

There was an operating cash inflow[3] of £1,719m (2011 £69m) reflecting advances received on the Omani and Saudi contract awards. These were partially offset by the utilisation of advances on the European Typhoon programme and costs against the provision on the Omani OPV programme.

Operational performance

Military Air & Information

Deliveries of Typhoon Tranche 2 aircraft to the four European partner nations totalled 46 in the year. At the end of 2012, cumulative aircraft deliveries to the four nations were 169 of the contracted 236. The first ten Tranche 3 front fuselage sub-assemblies were manufactured during the year. Manufacture of sub-assemblies continues in advance of recommencement of deliveries of Typhoon aircraft to Saudi Arabia in 2013.

In December 2012, a £2.5bn contract was awarded for the supply of 12 Typhoon and eight Hawk aircraft, associated training, and support to the Royal Air Force of Oman.

The business continues to support its UK and European customers' Typhoon and Tornado aircraft, and their operational commitments through availability-based service contracts and support operations. Orders of £668m were received in the year, including a contract worth £446m for Typhoon support operations across Germany, Italy, Spain and the UK. Support volumes on Tornado are expected to decline as the number of aircraft and flying hours reduce in advance of the out-of-service date of April 2019.

Delivery of the first F-35 Lightning II aircraft was accepted by the UK MoD. The business has delivered a further 42 production aircraft fuselage assemblies to Lockheed Martin. Interim funding of £234m for the fifth and sixth Low-Rate Initial Production contracts was secured in the year and negotiations continue in respect of final funding.

Support continues to be provided to operators of Hawk trainer aircraft around the world. In partnership with Hindustan Aeronautics Limited, production of 66 Batch 1 Hawk aircraft has been completed in India. Deliveries of materials and equipment in support of licence production of the 57 Batch 2 aircraft continue and aircraft assembly in India is ongoing. The business has provided an initial response to a request for proposal for an additional 20 aircraft to India.

Following the 2011 government-to-government Memorandum of Understanding, BAE Systems and Dassault Aviation have jointly secured an order from the UK and French governments for a Future Combat Air System demonstration programme preparation phase to plan how to mature and demonstrate critical technology and operational aspects for an Unmanned Combat Air System.

1 Including share of equity accounted investments.
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3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.
5 Includes both Group-funded and customer-funded expenditure.

In the defence information domain, the Falcon secure deployable communication system is now in service with the British Army and RAF.

Under a continuing focus on cost reduction and efficiency, there has been a net headcount[1] reduction of approximately 1,400 in the year.

Maritime

Cumulative savings of £342m have been reported to the MoD against commitments made under the 15-year Terms of Business Agreement (ToBA), significantly ahead of target. In line with the ToBA, the Group is progressing discussions with the MoD regarding future shipbuilding strategy after completion of block build for the Royal Navy's new aircraft carriers, and as the business transitions to the design and manufacture phase of the Type 26 Global Combat Ship.

The largest hull section of the first of the Royal Navy's new aircraft carriers, the Queen Elizabeth, has been delivered to Rosyth for assembly with the other completed hull sections. Block manufacture for the second ship, Prince of Wales, is well underway. BAE Systems and its Aircraft Carrier Alliance partners are working to finalise the detailed design changes required for operation of the short take-off and vertical landing variant of F-35 Lightning II on the carriers.

Defender, the fifth Type 45 destroyer, was accepted by the Royal Navy in July. The final ship, Duncan, has undertaken her sea trials and is on schedule for delivery in 2013. The Type 45 support contract met all ship deployment dates during the year.

Settlement with the Government of the Republic of Trinidad and Tobago, in respect of the cancelled OPV programme, was reached in November at an amount consistent with provisions held. In January 2013, £101m of the £131m cash settlement was paid, with the remainder due in May 2013. Following the agreement in December 2011 for the sale of the OPVs to the Brazilian Navy, the first two vessels were delivered in the year, with the third ship due for delivery in 2013.

Following an incident at sea during gunnery trials on the first Khareef Class corvette for Oman, detailed engineering, schedule and contract reviews have resulted in revised delivery dates for the ships. This has resulted in an increase in costs to complete the contract. The ships are expected to be delivered in 2013 and 2014.

The Type 26 Global Combat Ship assessment phase contract continues and is intended to be completed by the end of 2014. The Type 26 is planned to replace the Royal Navy's Type 23 frigates.

The warship support modernisation initiative contract, for delivery of services at Portsmouth Naval Base, continues to exceed contract performance. A new maritime support delivery framework will replace the existing contract in 2013.

The Advanced Radar Target Indication Situational Awareness Navigation (ARTISAN) 3-D radar successfully passed its factory acceptance test and the first of class has been fitted to HMS Iron Duke, a Type 23 frigate. The programme continues on track towards full production.

The Maritime Composite Training System, a shore-based warfare operator training solution, was declared ready for training by the Royal Navy in August having completed a year of initial training. Over 3,000 Royal Navy personnel have now been trained through the facility.

The Sting Ray lightweight torpedo delivery contract for the Norwegian government was completed in December.

Ambush, the second of class Astute submarine for the Royal Navy, departed for sea trials in the second half of the year. The operational handovers of both HMS Astute, the first of class, and Ambush are planned for 2013. Pricing for the fourth boat has been agreed with the customer and long lead procurement has commenced on the sixth and seventh boats.

BAE Systems secured a further £383m of funding from the UK MoD for the design and development phase of the Successor submarine programme, to replace the Vanguard Class fleet, and now has approximately 1,000 people engaged on the programme.

Combat Vehicles (UK)

The Terrier combat engineer vehicle contract concluded its reliability growth confirmation trials, which identified a number of required engineering changes. This has resulted in an increase in costs to complete the contract. Final trials are complete and deliveries of the 60 vehicles will commence in 2013.

Following delivery of the Terrier vehicles, the Newcastle facility will close, and support to Terrier and existing vehicles used by the British Army customer will be provided from the remaining facility at Telford and satellite offices.

Looking forward

Platforms & Services (UK) has a strong order backlog of long-term committed programmes and an enduring support business.

In Military Air & Information, sales are underpinned by military aircraft production on Typhoon, Hawk and F-35 Lightning II, and in-service support for existing and legacy combat and trainer aircraft. There are significant opportunities to secure future Typhoon export contracts to Malaysia, the United Arab Emirates and Saudi Arabia.

In Maritime, sales are underpinned by the Queen Elizabeth Class carrier and Astute Class submarine manufacturing programmes, the 15-year ToBA, the maritime support delivery framework, and the design of the Successor submarine and Type 26. The through-life support of these platforms and Type 45, together with their associated command and combat systems, provides sustainable business in technical services and mid-life upgrades.

In Combat Vehicles (UK), sales beyond the Terrier programme depend upon through-life support of legacy platforms.

REPORTING SEGMENTS: PLATFORMS & SERVICES (INTERNATIONAL)

Platforms & Services (International), with 15,500 employees[1], comprises the Group's businesses in Saudi Arabia, Australia, India and Oman, together with its 37.5% interest in the pan-European MBDA joint venture.

Operational key points

- Salam price escalation negotiations ongoing
- £5.0bn of orders received under the Saudi British Defence Co-operation Programme (SBDCP) for training aircraft and support to the end of 2016
- First Landing Helicopter Dock hull arrived in Australia for completion and second hull launched in Spain
- MBDA export order for MICA air-to-air missiles to India

Financial key points

- Order backlog[1] increased reflecting multi-year support and training awards under the SBDCP
- Like-for-like increase in sales[1] of 9% on increased support activity on the Salam Typhoon programme and weapons deliveries under the Tornado Sustainment Programme (TSP)
- Strong operating cash flow[3] reflecting acceleration of advances on TSP

	2012	2011	2010
Funded order intake[1]	**£5,266m**	£3,319m	£2,694m
Order backlog[1]	**£9.3bn**	£8.3bn	£9.1bn
Sales[1]	**£4,071m**	£3,794m	£4,325m
Underlying EBITA[2]	**£417m**	£449m	£449m
Return on sales	**10.2%**	11.8%	10.4%
Cash inflow[3]	**£506m**	£80m	£190m

Financial performance

Order intake[1] increased to £5.3bn (2011 £3.3bn) reflecting the award of orders for continuing support of the operational capability and training of the Saudi armed forces under the SBDCP to the end of 2016. Contracts were previously let on an annual basis.

Sales[1] in 2012 were £4.1bn, 9% higher than 2011 on a like-for-like basis, reflecting increased support activity on the Salam Typhoon programme and weapons deliveries under the TSP.

Underlying EBITA[2] was £417m (2011 £449m). Return on sales reduced to 10.2% (2011 11.8%) as 2011 benefited from strong performance and risk reduction on the Tornado upgrade and core support programmes in Saudi Arabia.

Operating cash inflow[3] of £506m (2011 £80m) reflected acceleration of advances on TSP.

Operational performance

Saudi Arabia

Through the entry into service of Typhoon and the continued development of the in-country industrial base, the Group remains committed to developing a greater indigenous capability in Saudi Arabia.

On the Salam programme, UK final assembly of the remaining 48 of the 72 Typhoon aircraft has commenced and deliveries are expected to resume in 2013. Work to expand the multi-role capabilities of the Royal Saudi Air Force (RSAF) Typhoon is progressing to schedule.

The initial three-year Typhoon support contract finished at the end of June and two subsequent six-month extensions have been secured. Discussions continue with the customer on the next five years of support.

Discussions on Typhoon price escalation with the Saudi Arabian government remain ongoing. Negotiations are also ongoing for the provision of maintenance and upgrade facilities in-Kingdom, and further capability enhancement of the aircraft.

The business continues to support the operational capability of both the RSAF and Royal Saudi Naval Forces (RSNF). A £1.6bn contract was awarded in May to upgrade the RSAF's aircrew training aircraft, involving the supply of, and initial support for, Hawk advanced jet trainer and Pilatus PC-21 training aircraft. The business was also awarded orders totalling £3.4bn for support to the end of 2016, including the provision of manpower, logistics and training to the RSAF.

Under the TSP, the upgrade of the RSAF Tornado fleet is complete, with all of the contracted aircraft having been delivered back into the RSAF fleet. Delivery of Storm Shadow missiles to the RSAF under the TSP is progressing in line with the agreed programme schedule.

Work continues on the first ship re-fit on the minehunter mid-life update programme. The ship is due to be handed back to the RSNF customer during the second half of 2013.

On the C4I (Command, Control, Communications, Computers & Intelligence) programme, the business continues to seek an acceptable closure of the contract with the customer.

Australia

Integration of the first of two Landing Helicopter Docks commenced at the Williamstown shipyard following the arrival of the hull from subcontractor Navantia in Spain. The second hull was launched at Navantia's Ferrol shipyard.

1 Including share of equity accounted investments.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 6).
3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.

A total of nine hull blocks have been constructed and delivered under the A$209m (£134m) Air Warfare Destroyer contract, completing the Group's involvement in the first two ships of the three being built.

In 2012, the business completed the multi-year project to modernise 431 M113 armoured personnel carriers for the Australian Army.

The first of seven Royal Australian Navy ANZAC Class frigates is being upgraded with anti-ship missile defence capability at the Henderson shipyard under a A$267m (£171m) contract signed in January 2012.

The business has been selected as the preferred tenderer to provide ongoing in-service support for the Royal Australian Air Force's Hawk Lead-In Fighter fleet and contract negotiations are ongoing.

The business was awarded an in-service electronic warfare support contract for the Wedgetail airborne early warning and control aircraft fleet to 2015 with a value up to A$68m (£43m).

Whilst the business submitted a bid for the next-generation Battlespace Communications System, the decision was taken to withdraw from this competition after a breach of tender protocols had occurred during its participation in the initial tender process.

India
Following a strategic review of the Defence Land Systems India (DLSI) joint venture, it has been jointly agreed that Mahindra & Mahindra will acquire BAE Systems' 26% shareholding in DLSI. This decision is a reflection of the shareholders' belief that they can best meet customer requirements and address market opportunities on a case-by-case basis, including continuing to explore opportunities for co-operating on specific defence projects.

BAE Systems is participating as a subcontractor to Bharat Electronics Limited (BEL) on the Tactical Communications Systems programme for the Indian military, for which BEL has been selected as one of two design authorities.

The Indian government has issued a Letter of Request to the US government under the US Foreign Military Sales process for the supply of 145 M777 howitzers for the Indian Army.

Together with its Eurofighter industry partners, the Group continues to monitor the Medium Multi-Role Combat Aircraft competition and stands ready to support the Indian government's procurement process.

The Group has received a request for proposal for a third batch of Hawk advanced jet trainer aircraft for the Indian Air Force.

Oman
The contract for the supply of Typhoon and Hawk aircraft awarded in December 2012 builds on the close partnership with the Omani armed forces and provides the platform to ensure this relationship is further developed. The Group has a long history of working closely with the Omani armed forces, and currently supports their existing air, land and maritime platforms, such as air defence radars, Challenger tanks, and Jaguar and Hawk aircraft.

MBDA
In the export market, a significant order was received from India in early 2012 for MICA air-to-air missiles as part of the Indian Air Force's Mirage 2000 upgrade.

In the domestic market, the business secured an important support contract for the Principal Anti-Air Missile System and a development contract for the Future Local Anti-Air Defence System. The business continues to pursue the Anglo-French joint development and production opportunity for the Future Anti-Ship Guided Weapon – Anti-Navire Léger.

Development programmes continue to progress well. The Meteor beyond visual range air-to-air missile successfully concluded its guided firing programme.

Looking forward

In the Kingdom of Saudi Arabia, the Group seeks to build upon its long-term presence through delivering current programmes and industrialisation, and developing new business in support of the Saudi military and security forces.

Following agreement of the training aircraft and support orders under the SBDCP in 2012, the focus turns towards mobilising activities on the next phases of these programmes.

In Australia, BAE Systems will continue to support the Department of Defence by working with the customer to deliver cost and service improvements. The business continues to explore and secure opportunities in adjacent markets, including commercial maritime repair and support, and commercial fabrication for the natural resources industry.

In India, significant aircraft and artillery opportunities continue to be pursued.

In MBDA, whilst domestic budgetary pressures continue, export markets are anticipated to grow, potentially benefiting from significant military aircraft procurements.

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December

	Notes	2012 £m	2012 Total £m	2011 £m	2011 Total £m
Continuing operations					
Combined sales of Group and share of equity accounted investments	2		**17,834**		19,154
Less: share of sales of equity accounted investments	2		**(1,214)**		(1,384)
Revenue	2		**16,620**		17,770
Operating costs			**(15,353)**		(16,478)
Other income			**280**		157
Group operating profit			**1,547**		1,449
Share of results of equity accounted investments			**93**		131
Underlying EBITA[1]		**1,895**		2,025	
Non-recurring items[2]		**103**		(78)	
EBITA		**1,998**		1,947	
Amortisation		**(226)**		(239)	
Impairment		**(86)**		(109)	
Financial (expense)/income of equity accounted investments		**(4)**		8	
Taxation expense of equity accounted investments		**(42)**		(27)	
Operating profit	2		**1,640**		1,580
Financial income		**1,326**		1,294	
Financial expense		**(1,597)**		(1,408)	
Finance costs	3		**(271)**		(114)
Profit before taxation			**1,369**		1,466
Taxation expense			**(295)**		(206)
Profit for the year – continuing operations			**1,074**		1,260
Profit/(loss) for the year – discontinued operations			**5**		(4)
Profit for the year			**1,079**		1,256
Attributable to:					
Equity shareholders			**1,068**		1,240
Non-controlling interests			**11**		16
			1,079		1,256
Earnings per share	4				
Basic earnings per share			**33.0p**		36.9p
Diluted earnings per share			**32.8p**		36.7p
Earnings per share – continuing operations					
Basic earnings per share			**32.8p**		37.0p
Diluted earnings per share			**32.6p**		36.8p

1 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
2 Comprises profit on disposal of businesses £103m (2011 loss £29m) and regulatory penalties £nil (2011 £49m).

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December

	2012			2011		
	Other reserves £m	Retained earnings £m	Total £m	Other reserves £m	Retained earnings £m	Total £m
Profit for the year	–	1,079	1,079	–	1,256	1,256
Other comprehensive income						
Items that will not be reclassified to the income statement:						
Net actuarial losses on defined benefit pension schemes:						
Subsidiaries	–	(796)	(796)	–	(1,522)	(1,522)
Equity accounted investments	–	(84)	(84)	–	(45)	(45)
Tax on items that will not be reclassified to the income statement	–	173	173	–	387	387
Items that may be reclassified to the income statement:						
Currency translation on foreign currency net investments:						
Subsidiaries	(164)	–	(164)	(19)	–	(19)
Equity accounted investments	(25)	–	(25)	(17)	–	(17)
Reclassification of cumulative currency translation reserve on disposal	(97)	–	(97)	(14)	–	(14)
Amounts charged to hedging reserve	(21)	–	(21)	(56)	–	(56)
Fair value movements on available-for-sale investments	–	–	–	–	5	5
Reclassification of fair value movements on available-for-sale investments	–	–	–	–	(21)	(21)
Tax on items that may be reclassified to the income statement	5	–	5	17	–	17
Total other comprehensive income for the year (net of tax)	(302)	(707)	(1,009)	(89)	(1,196)	(1,285)
Total comprehensive income for the year	(302)	372	70	(89)	60	(29)
Attributable to:						
Equity shareholders	(302)	361	59	(89)	44	(45)
Non-controlling interests	–	11	11	–	16	16
	(302)	372	70	(89)	60	(29)

NOTES TO THE ACCOUNTS – INCOME STATEMENT

1. Preparation

The consolidated financial statements of BAE Systems plc have been prepared in accordance with EU-endorsed International Financial Reporting Standards (IFRS) and the Companies Act 2006 applicable to companies reporting under IFRS.

With effect from 1 January 2012, the Group early adopted amendments to IAS 1, Presentation of Financial Statements, which requires items within Other Comprehensive Income that may be reclassified to the income statement to be grouped together. This amendment is concerned with disclosure only and has no impact on the reported results or financial position of the Group.

There were no other changes in accounting policies during the year.

The consolidated financial statements are presented in pounds sterling and, unless stated otherwise, rounded to the nearest million. They have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets, and other relevant financial assets and financial liabilities (including derivative instruments).

2. Segmental analysis

Sales and revenue by reporting segment

	Combined sales of Group and share of equity accounted investments		Less: sales by equity accounted investments		Add: sales to equity accounted investments		Revenue	
	2012 £m	2011 £m	**2012 £m**	2011 £m	**2012 £m**	2011 £m	**2012 £m**	2011 £m
Electronic Systems	**2,507**	2,645	**(52)**	(49)	**52**	49	**2,507**	2,645
Cyber & Intelligence	**1,402**	1,399	**–**	–	**–**	–	**1,402**	1,399
Platforms & Services (US)	**4,539**	5,305	**(70)**	(52)	**1**	2	**4,470**	5,255
Platforms & Services (UK)	**5,646**	6,258	**(1,430)**	(1,476)	**1,346**	1,374	**5,562**	6,156
Platforms & Services (International)	**4,071**	3,794	**(830)**	(1,039)	**–**	–	**3,241**	2,755
HQ	**267**	233	**(267)**	(233)	**–**	–	**–**	–
	18,432	19,634	**(2,649)**	(2,849)	**1,399**	1,425	**17,182**	18,210
Intra-group sales/revenue	**(598)**	(480)	**2**	3	**34**	37	**(562)**	(440)
	17,834	19,154	**(2,647)**	(2,846)	**1,433**	1,462	**16,620**	17,770

Reporting segment result

	Underlying EBITA[1]		Non-recurring items[2]		Amortisation of intangible assets		Impairment of intangible assets		Reporting segment result	
	2012 £m	2011 £m	**2012 £m**	2011 £m	**2012 £m**	2011 £m	**2012 £m**	2011 £m	**2012 £m**	2011 £m
Electronic Systems	**356**	386	**–**	–	**(22)**	(15)	**(2)**	–	**332**	371
Cyber & Intelligence	**124**	136	**–**	–	**(76)**	(64)	**–**	–	**48**	72
Platforms & Services (US)	**394**	478	**103**	(29)	**(92)**	(118)	**(84)**	(75)	**321**	256
Platforms & Services (UK)	**689**	658	**–**	–	**(28)**	(32)	**–**	(34)	**661**	592
Platforms & Services (International)	**417**	449	**–**	–	**(8)**	(10)	**–**	–	**409**	439
HQ	**(85)**	(82)	**–**	(49)	**–**	–	**–**	–	**(85)**	(131)
	1,895	2,025	**103**	(78)	**(226)**	(239)	**(86)**	(109)	**1,686**	1,599
Financial (expense)/income of equity accounted investments									**(4)**	8
Taxation expense of equity accounted investments									**(42)**	(27)
Operating profit									**1,640**	1,580
Finance costs									**(271)**	(114)
Profit before taxation									**1,369**	1,466
Taxation expense									**(295)**	(206)
Profit for the year – continuing operations									**1,074**	1,260

1 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
2 Comprises profit on disposal of businesses £103m (2011 loss £29m) and regulatory penalties £nil (2011 £49m).

3. Finance costs

	2012 £m	2011 £m
Interest income	**39**	30
Income from financial assets at fair value through profit or loss	**–**	4
Expected return on pension scheme assets	**874**	989
Reclassification of fair value movements on available-for-sale investments	**–**	21
Gain on remeasurement of financial instruments at fair value through profit or loss	**280**	174
Foreign exchange gains	**133**	76
Financial income	**1,326**	1,294
Interest expense on bonds and other financial instruments[1]	**(187)**	(204)
Charges relating to early redemption of debt	**–**	(13)
Facility fees	**(7)**	(7)
Net present value adjustments	**(56)**	(33)
Interest charge on pension scheme liabilities	**(929)**	(965)
Loss on remeasurement of financial instruments at fair value through profit or loss	**(250)**	(163)
Foreign exchange losses	**(168)**	(23)
Financial expense	**(1,597)**	(1,408)
Net finance costs	**(271)**	(114)

Additional analysis

	2012 £m	2011 £m
Net finance costs:		
Group	**(271)**	(114)
Share of equity accounted investments	**(4)**	8
	(275)	(106)
Analysed as:		
Underlying interest (expense)/income:		
Group[1]	**(211)**	(210)
Share of equity accounted investments	**7**	11
	(204)	(199)
Other:		
Group:		
Net financing (charge)/credit on pensions	**(55)**	24
Market value and foreign exchange adjustments on financial instruments and investments	**(5)**	85
Charges relating to early redemption of debt	**–**	(13)
Share of equity accounted investments	**(11)**	(3)
	(275)	(106)

1 2011 restated to exclude £13m of pre-tax charges relating to early redemption of debt, with £28m that would have been incurred in future years remaining within underlying interest.

NOTES TO THE ACCOUNTS – INCOME STATEMENT *(continued)*

4. Earnings per share

	2012			2011		
	£m	Basic pence per share	Diluted pence per share	£m	Basic pence per share	Diluted pence per share
Profit for the year attributable to equity shareholders	**1,068**	**33.0**	**32.8**	1,240	36.9	36.7
Represented by:						
Continuing operations	**1,063**	**32.8**	**32.6**	1,244	37.0	36.8
Discontinued operations	**5**	**0.2**	**0.2**	(4)	(0.1)	(0.1)
(Deduct)/add back:						
(Profit)/loss on disposal of businesses	**(103)**			29		
Regulatory penalties	**–**			49		
Net financing charge/(credit) on pensions, post tax	**50**			(18)		
Market value and foreign exchange adjustments on financial instruments and investments, post tax	**4**			(61)		
Charges relating to early redemption of debt, post tax	**–**			10		
Amortisation and impairment of intangible assets, post tax	**192**			188		
Impairment of goodwill	**57**			94		
Underlying earnings, post tax	**1,268**	**39.1**	**39.0**	1,531	45.5	45.3
Represented by:						
Continuing operations	**1,263**	**38.9**	**38.8**	1,535	45.6	45.4
Discontinued operations	**5**	**0.2**	**0.2**	(4)	(0.1)	(0.1)
	1,268	**39.1**	**39.0**	1,531	45.5	45.3
Underlying earnings excluding R&D tax benefit (2011 £197m)				1,334	39.6	39.4
Represented by:						
Continuing operations				1,338	39.7	39.5
Discontinued operations				(4)	(0.1)	(0.1)
				1,334	39.6	39.4

	2012 Millions	2012 Millions	2011 Millions	2011 Millions
Weighted average number of shares used in calculating basic earnings per share	**3,244**	**3,244**	3,365	3,365
Incremental shares in respect of employee share schemes		**14**		17
Weighted average number of shares used in calculating diluted earnings per share		**3,258**		3,382

Underlying earnings per share is presented in addition to that required by IAS 33, Earnings per Share, to align the adjusted earnings measure with the performance measure reviewed by the directors. The directors consider that this gives a more appropriate indication of underlying performance.

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December

	Notes	2012 £m	2011 £m
Profit for the year		**1,079**	1,256
Taxation expense		**296**	211
Share of results of equity accounted investments		**(93)**	(131)
Net finance costs		**271**	117
Depreciation, amortisation and impairment		**669**	751
Profit on disposal of property, plant and equipment		**(7)**	(17)
Profit on disposal of investment property		**(12)**	(21)
(Profit)/loss on disposal of businesses		**(103)**	15
Cost of equity-settled employee share schemes		**57**	68
Movements in provisions		**(224)**	(148)
Decrease in liabilities for retirement benefit obligations		**(859)**	(287)
Decrease/(increase) in working capital:			
Inventories		**6**	(85)
Trade and other receivables		**447**	191
Trade and other payables		**931**	(969)
Cash inflow from operating activities		**2,458**	951
Interest paid		**(170)**	(212)
Taxation paid		**(115)**	(257)
Net cash inflow from operating activities		**2,173**	482
Dividends received from equity accounted investments		**94**	88
Interest received		**23**	32
Income from financial assets at fair value through profit or loss		**–**	4
Purchases of property, plant and equipment, and investment property		**(359)**	(359)
Purchases of intangible assets		**(43)**	(24)
Proceeds from sale of property, plant and equipment, and investment property		**115**	115
Purchase of subsidiary undertakings (net of cash acquired)		**(5)**	(532)
Equity accounted investment funding		**(6)**	(1)
Proceeds from sale of subsidiary undertakings (net of cash disposed)		**101**	124
Proceeds from sale of financial assets at fair value through profit or loss		**–**	152
Proceeds from sale of other investments		**–**	1
Net proceeds from sale of other deposits/securities		**–**	265
Net cash outflow from investing activities		**(80)**	(135)
Purchase of treasury shares		**–**	(503)
Purchase of own shares		**(16)**	(6)
Equity dividends paid	7	**(620)**	(606)
Dividends paid to non-controlling interests		**(11)**	(22)
Cash outflow from matured derivative financial instruments		**(119)**	(34)
Cash outflow from movement in cash collateral		**(2)**	–
Cash inflow from loans		**1,863**	2,693
Cash outflow from repayment of loans		**(1,975)**	(2,541)
Net cash outflow from financing activities		**(880)**	(1,019)
Net increase/(decrease) in cash and cash equivalents[1]		**1,213**	(672)
Cash and cash equivalents at 1 January		**2,136**	2,802
Effect of foreign exchange rate changes on cash and cash equivalents		**(15)**	6
Cash and cash equivalents at 31 December		**3,334**	2,136
Comprising:			
Cash and cash equivalents[2]		**3,355**	2,141
Overdrafts		**(21)**	(5)
Cash and cash equivalents at 31 December		**3,334**	2,136

1 Includes net cash inflow from discontinued operations of £2m (2011 £51m).
2 Includes £nil (2011 £403m) of cash held in Trust for the benefit of the Group's main pension scheme (see note 5).

CONSOLIDATED BALANCE SHEET

as at 31 December

	Notes	2012 £m	2011 £m
Non-current assets			
Intangible assets		**10,928**	11,465
Property, plant and equipment		**2,285**	2,496
Investment property		**122**	130
Equity accounted investments		**265**	783
Other investments		**5**	5
Other receivables		**254**	314
Other financial assets		**62**	118
Deferred tax assets		**1,375**	1,409
		15,296	16,720
Current assets			
Inventories		**655**	716
Trade and other receivables including amounts due from customers for contract work		**2,873**	3,369
Current tax		**11**	60
Other financial assets		**64**	77
Cash and cash equivalents		**3,355**	2,141
Assets held for sale		**20**	18
		6,978	6,381
Total assets		**22,274**	23,101
Non-current liabilities			
Loans		**(2,967)**	(2,682)
Trade and other payables		**(1,481)**	(571)
Retirement benefit obligations	5	**(4,607)**	(4,673)
Other financial liabilities		**(66)**	(74)
Deferred tax liabilities		**(13)**	(26)
Provisions		**(449)**	(501)
		(9,583)	(8,527)
Current liabilities			
Loans and overdrafts		**(21)**	(518)
Trade and other payables		**(8,067)**	(8,531)
Other financial liabilities		**(88)**	(284)
Current tax		**(422)**	(468)
Provisions		**(297)**	(453)
Liabilities held for sale		**(22)**	(21)
		(8,917)	(10,275)
Total liabilities		**(18,500)**	(18,802)
Net assets		**3,774**	4,299
Capital and reserves			
Issued share capital		**90**	90
Share premium		**1,249**	1,249
Other reserves		**5,079**	5,381
Retained earnings – deficit		**(2,698)**	(2,480)
Total equity attributable to equity holders of the parent		**3,720**	4,240
Non-controlling interests		**54**	59
Total equity		**3,774**	4,299

Approved by the Board on 20 February 2013 and signed on its behalf by:

I G King
Chief Executive

P J Lynas
Group Finance Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December

	Attributable to equity holders of the parent						
	Issued share capital £m	Share premium £m	Other reserves £m	Retained earnings £m	Total £m	Non-controlling interests £m	Total equity £m
At 1 January 2012	90	1,249	5,381	(2,480)	4,240	59	4,299
Profit for the year	–	–	–	1,068	1,068	11	1,079
Total other comprehensive income for the year	–	–	(302)	(707)	(1,009)	–	(1,009)
Share-based payments	–	–	–	57	57	–	57
Purchase of own shares	–	–	–	(16)	(16)	–	(16)
Ordinary share dividends	–	–	–	(620)	(620)	(11)	(631)
Other	–	–	–	–	–	(5)	(5)
At 31 December 2012	**90**	**1,249**	**5,079**	**(2,698)**	**3,720**	**54**	**3,774**
At 1 January 2011	90	1,249	5,470	(1,477)	5,332	71	5,403
Profit for the year	–	–	–	1,240	1,240	16	1,256
Total other comprehensive income for the year	–	–	(89)	(1,196)	(1,285)	–	(1,285)
Share-based payments	–	–	–	68	68	–	68
Purchase of own shares	–	–	–	(6)	(6)	–	(6)
Purchase of treasury shares	–	–	–	(503)	(503)	–	(503)
Ordinary share dividends	–	–	–	(606)	(606)	(22)	(628)
Other	–	–	–	–	–	(6)	(6)
At 31 December 2011	90	1,249	5,381	(2,480)	4,240	59	4,299

NOTES TO THE ACCOUNTS – BALANCE SHEET

5. Retirement benefit obligations

	UK £m	US and other £m	Total £m
Total IAS 19 deficit at 1 January 2012	(4,676)	(909)	**(5,585)**
Actual return on assets above expected return	478	211	**689**
Increase in liabilities due to changes in assumptions and experience	(1,307)	(416)	**(1,723)**
Additional contributions in excess of service cost	698	–	**698**
Recurring contributions in excess of service cost	145	92	**237**
Past service cost	(26)	(1)	**(27)**
Curtailment gains	–	26	**26**
Net financing (charge)/credit	(107)	35	**(72)**
Foreign exchange adjustment	–	38	**38**
Movement in US healthcare schemes	–	11	**11**
Total IAS 19 deficit at 31 December 2012	**(4,795)**	**(913)**	**(5,708)**
Allocated to equity accounted investments and other participating employers	1,148	–	**1,148**
Group's share of IAS 19 deficit excluding Group's share of amounts allocated to equity accounted investments and other participating employers at 31 December 2012	**(3,647)**	**(913)**	**(4,560)**
Represented by:			
Pension prepayments (within trade and other receivables)	–	47	**47**
Retirement benefit obligations	(3,647)	(960)	**(4,607)**
	(3,647)	**(913)**	**(4,560)**

Certain of the Group's equity accounted investments participate in the Group's defined benefit schemes as well as Airbus SAS, the Group's share of which was disposed of in 2006. As these schemes are multi-employer schemes, the Group has allocated an appropriate share of the IAS 19, Employee Benefits, pension deficit to the equity accounted investments and Airbus SAS based upon a consistent allocation method intended to reflect a reasonable approximation of their share of the deficit. The Group's share of the IAS 19 pension deficit allocated to the equity accounted investments is included in the balance sheet within equity accounted investments. In the event that an employer who participates in the Group's pension schemes fails or cannot be compelled to fulfil its obligations as a participating employer, the remaining participating employers are obliged to collectively take on its obligations. The Group considers the likelihood of this event arising as remote.

The Group's share of the IAS 19 deficit excluding the Group's share of amounts allocated to equity accounted investments and other participating employers is £3.4bn (31 December 2011 £3.4bn) after tax.

Life expectancy

In February 2013, with the agreement of the Company, the trustees of the BAE Systems 2000 Pension Plan (2000 Plan) entered into an arrangement with Legal & General to insure against longevity risk for the current pensioner population, covering £2.7bn of pension scheme liabilities. This will reduce the funding volatility relating to increasing life expectancy.

Contributions

During the year, a total of £428m was paid into the BAE Systems Pension Scheme (Main Scheme) and 2000 Plan from the Trust (see below). In addition, £75m was contributed by the Group to the Main Scheme upon sale of certain properties. The total Group contributions made to the defined benefit schemes in the year ended 31 December 2012 were £1,029m (2011 £515m) excluding those amounts allocated to equity accounted investments and participating employers of £128m (2011 £70m).

In 2013, the Group expects to make regular contributions at a similar level to the recurring contributions made in 2012 and additional contributions, such that total deficit funding, in excess of service cost, is expected to be approximately £0.4bn.

The Group incurred a charge in respect of the cash contributions of £129m (2011 £119m) paid to defined contribution schemes for employees.

During the year, the Group contributed £25m into Trust for the benefit of the 2000 Plan. On 27 September, £387m was paid out of the Trust into the Main Scheme and £25m was paid out of the Trust into the 2000 Plan. In December, the remaining £16m was paid into the Main Scheme. These payments are included within additional contributions in excess of service cost in the table above. The Group considers the contributions made to the Trust to be equivalent to the other lump sum contributions it makes into the Group's pension schemes and, accordingly, presents below a definition of the pension deficit including them.

	2012 £m	2011 £m
Group's share of IAS 19 deficit, net	**(4,560)**	(4,620)
Assets held in Trust	**–**	403
Pension deficit (as defined by the Group)	**(4,560)**	(4,217)

NOTES TO THE ACCOUNTS – OTHER INFORMATION

6. Acquisition and disposal of subsidiaries

Subsidiaries disposed of during 2012 – continuing operations

In March, the Group completed the sale of its BAE Systems Safety Products Inc. and Schroth Safety Products GmbH businesses (Safety Products) in the US and Germany for cash consideration of approximately $32m (£21m).

In July, the US-based Safariland, LLC (Safariland) business was sold for cash consideration (after adjustment) of approximately $124m (£78m).

Also in July, the Group sold the assets comprising its BAE Systems Tensylon High Performance Materials Inc. (Tensylon) business for cash consideration of $18m (£12m).

Summary

	Safariland £m	Other £m	Total £m
Cash consideration	78	33	111
Transaction costs paid	(1)	(2)	(3)
Cash proceeds	**77**	**31**	**108**
Transaction costs accrued	(1)	–	(1)
Net proceeds	**76**	**31**	**107**
Net assets disposed:			
Intangible assets	(23)	(12)	(35)
Property, plant and equipment	(15)	(4)	(19)
Inventories	(16)	(14)	(30)
Trade and other receivables	(22)	(3)	(25)
Deferred tax	(2)	6	4
Trade and other payables	13	2	15
Cash and cash equivalents	(10)	(1)	(11)
	(75)	**(26)**	**(101)**
Cumulative currency translation gain	84	13	97
Profit on disposal of businesses – continuing operations	**85**	**18**	**103**

Safariland and Tensylon were written down to fair value less costs to sell prior to their disposal incurring impairment charges to intangible assets of £48m and £12m, respectively.

Subsidiaries acquired during 2011

The Group acquired L-1 Identity Solutions, Inc.'s Intelligence Services Group (L-1 ISG), Norkom Group plc (Norkom), ETI A/S (ETI), Fairchild Imaging, Inc. (Fairchild) and stratsec.net Pty Limited (stratsec). With the exception of Fairchild, the Group acquired 100% of the shares of these entities. The Group acquired the remaining 91.3% interest in Fairchild which it did not already own.

If the acquisitions had occurred on 1 January 2011, combined sales of Group and share of equity accounted investments would have been £19.2bn, revenue £17.8bn and profit £1,252m from continuing operations for the year ended 31 December 2011.

For all acquisitions made during 2011, fair values were finalised in 2012. In accordance with IFRS 3, Business Combinations, the Group has adjusted the fair values attributable to the Norkom and ETI acquisitions during 2012. The net increase in goodwill of £2m is not material to the consolidated accounts and, as such, the Group has not restated the balance sheet at 31 December 2011.

Material acquisitions

			Consolidated results for the period from acquisition to 31 December 2011		
Acquisition	Acquisition date	Total consideration £m	Revenue £m	EBITA[1] £m	Loss after tax[2] £m
L-1 ISG	15 February 2011	180	112	8	(2)
Norkom	18 February 2011	177	42	9	(3)
ETI	21 March 2011	135	39	5	(9)

1 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense excluding integration costs.
2 Includes amortisation charges on acquired intangible assets totalling £39m.

NOTES TO THE ACCOUNTS – OTHER INFORMATION *(continued)*

7. Equity dividends

	2012 £m	2011 £m
Prior year final 11.3p dividend per ordinary share paid in the year (2011 10.5p)	367	359
Interim 7.8p dividend per ordinary share paid in the year (2011 7.5p)	253	247
	620	606

After the balance sheet date, the directors proposed a final dividend of 11.7p. The dividend, which is subject to shareholder approval, will be paid on 3 June 2013 to shareholders registered on 19 April 2013. The ex-dividend date is 17 April 2013.

Shareholders who do not at present participate in the Company's Dividend Reinvestment Plan and wish to receive the final dividend in shares rather than cash should complete a mandate form for the Dividend Reinvestment Plan and return it to the registrars no later than 10 May 2013.

8. Related party transactions

The Group has a related party relationship with its directors and key management personnel, equity accounted investments and pension plans.

Transactions occur with the equity accounted investments in the normal course of business, are priced on an arm's-length basis and settled on normal trade terms. The more significant transactions are disclosed below:

	Year ended 31 December 2012 £m	Year ended 31 December 2011 £m
Sales to related parties	1,433	1,462
Purchases from related parties	250	317

	31 December 2012 £m	31 December 2011 £m
Amounts owed by related parties	163	234
Amounts owed to related parties	708	1,161

9. Annual General Meeting

This year's Annual General Meeting will be held on 8 May 2013. Details of the resolutions to be proposed at that meeting will be included in the notice of Annual General Meeting that will be sent to shareholders at the end of March 2013.

10. Other information

The financial information for the year ended 31 December 2012 contained in this preliminary announcement was approved by the Board on 20 February 2013. This announcement does not constitute statutory accounts of the Company within the meaning of section 435 of the Companies Act 2006, but is derived from those accounts.

Statutory accounts for the year ended 31 December 2011 have been delivered to the Registrar of Companies. Statutory accounts for the year ended 31 December 2012 will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

The auditors have reported on those accounts. Their reports were not qualified, did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report, and did not contain a statement under section 498 (2) or (3) of the Companies Act 2006.

FOR MORE INFORMATION

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