Preliminary Announcement and Presentation 2009

Delivering Total Performance

BAE SYSTEMS

REAL PERFORMANCE. REAL ADVANTAGE.

Cover image:
Typhoon

RESULTS IN BRIEF, HIGHLIGHTS AND OUTLOOK

Results in brief

	2009	2008
Sales[1]	**£22,415m**	£18,543m
Underlying EBITA[2]	**£2,220m**	£1,897m
Operating profit	**£982m**	£1,718m
Underlying earnings[3] per share	**40.7p**	37.1p
Basic (loss)/earnings per share[4]	**(1.9)p**	49.6p
Order book[5]	**£46.9bn**	£46.5bn
Dividend per share	**16.0p**	14.5p
Cash inflow from operating activities	**£2,232m**	£2,009m
Net cash as defined by the Group[6]	**£403m**	£39m

Highlights

- Sales[1] increased by 21%
- Underlying EBITA[2] increased by 17%
- £261m accounting gain on US pension restructuring and £278m of regulatory penalties excluded from underlying EBITA[2]
- £973m of impairment charges largely relating to the ex-Armor Holdings business
- Underlying earnings[3] per share up 10% to 40.7p
- Dividend for the year increased by 10% to 16.0p per share
- £500m market purchase of shares to commence

Outlook

In 2010, we anticipate growth for three of our four operating groups, whilst at Land & Armaments return on sales will improve as rationalisation and efficiency programmes progress. In aggregate, and despite a planned lower level of land vehicle activity, the Group continues to expect growth for 2010 based on constant exchange rate assumptions.

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 4).
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 (loss)/earnings per share in accordance with International Accounting Standard 33.
5 Including share of equity accounted investments' order books and after the elimination of intra-group orders of £1.7bn (2008 £1.4bn).
6 See page 5.

PRELIMINARY RESULTS STATEMENT

"BAE Systems has evolved to become one of the world's leading defence companies and is well positioned to weather the pressures in its global markets."

The good operating performance of BAE Systems in 2009 reflects the good progress the Group has made in recent years, developing the business within a well-defined and consistently implemented strategic framework. That strategy underpins the Group's aim to deliver sustainable growth in shareholder value through a commitment to Total Performance for all its customers.

Earlier this month the Company announced that it had reached a global settlement with the US Department of Justice and the UK Serious Fraud Office in connection with their long running investigations. Under the agreement with the Department of Justice, which requires court approval, the Company will plead guilty to one charge of conspiring to make false statements to the US government in connection with certain regulatory filings and undertakings. The Company will pay a fine of $400m (£248m) and make additional commitments concerning its ongoing compliance. Under the agreement with the Serious Fraud Office, the Company will plead guilty to one charge of breach of duty to keep accounting records in relation to payments made to a former marketing adviser in Tanzania. The Company will pay an agreed penalty of £30m comprising a fine to be determined by the Court with the balance paid as a charitable payment for the benefit of Tanzania.

The Company very much regrets and accepts full responsibility for these past shortcomings. These settlements enable the Company to deal finally with significant legacy issues. In the years since the conduct referred to in the settlements occurred, the Company has systematically enhanced its compliance policies and processes with a view to ensuring that the Company is as widely recognised for responsible conduct as it is for high quality products and advanced technologies.

BAE Systems is a resilient business, well positioned to weather the pressures that result from the recent turbulence in global economies. The Group operates primarily in its seven home markets, and has a wide portfolio of products and capabilities serving defence customers across the air, land and sea domains. Many of the Group's programmes are subject to long-term contracts, and some include agreements designed to address and safeguard national capabilities.

Alongside its established defence-related activities, BAE Systems has a growing position in national security with a focus on information-based intelligence capabilities. The acquisition of Detica in September 2008 was a further step in the implementation of the Group's security strategy. BAE Systems is well placed to address opportunities in security markets, such as increasing focus on cyber threats.

The Group's geographic spread of business extends the diversity of its customer base. The strategy, to identify long-term sustainable markets around the globe and address those markets by building local industrial positions, is working to good effect. India has been identified as the Group's seventh home market and, in November, an agreement was signed with Mahindra & Mahindra to establish a joint venture in land systems.

Rapid changes in the nature and evolution of threats around the world have resulted in corresponding changes in priorities for many of the Group's customers. BAE Systems recognises that agility in addressing customers' requirements is becoming a key competitive discriminator.

Defence budgets in both the UK and the US are expected to come under further pressure, and with expectations of a more challenging business environment ahead, the focus on driving performance and efficiency in the business will be key. Cost reduction measures are being aggressively implemented across the Group.

US business
In the US, overall defence spending remains robust but the investment accounts, from which the Group derives significant business, are expected to be stressed by the continued cost of high tempo operations and rising manpower costs.

In April 2009, the US Secretary of Defense announced a reprioritisation of programmes that is expected to continue to shape US defence procurement. Many of BAE Systems' activities are well aligned to those announced priority changes. In February 2010, the US Quadrennial Defense Review was published along with the US defence budget for the Fiscal Year 2011 (FY11). The FY11 base budget identifies an increase of 3.4% and within this base budget the investment account allocations were at the upper end of the Group's planning assumptions.

The Group's high technology capabilities in the US are expected to continue to be in demand. The business has a strong record of innovation, rapidly generating advanced, but cost effective, solutions to address complex problems.

In June, BAE Systems completed the acquisition of Advanced Ceramics Research, Inc. for $14m (£9m). The acquisition supports BAE Systems' global Unmanned Aircraft Systems (UAS) strategy, adding small UAS platforms and ground segment capability to complement the Group's existing UAS capabilities.

A setback for the Group was the notification by the US Department of Defense in August 2009 and, following a re-evaluation of the bids, in February 2010 that a follow-on production contract for vehicles under the Family of Medium Tactical Vehicles (FMTV) programme had been lost.

UK and rest of world business
The outlook for UK defence spending remains difficult, but the Group has a large order book reflecting the firmly contracted long-term programmes that are a feature of BAE Systems' UK-based business.

The largest of those programmes, the Typhoon combat aircraft, is set for further growth with increasing deliveries to both the four European partner nations and to the Kingdom of Saudi Arabia.

BAE Systems is a leader in the provision of multi-year, capability-based, support solutions. Approximately 40% of BAE Systems' sales in 2009 are Readiness & Sustainment related activity. In addition to established relationships in the UK, the Kingdom of Saudi Arabia and Australia, BAE Systems seeks to migrate its Readiness & Sustainment capabilities to other markets.

New multi-year UK support contracts were awarded in the year totalling over £2bn. Such contracts included support and maintenance of Harrier and Typhoon aircraft in service with the Royal Air Force, the Type 45 anti-air warfare destroyer (the Group's first major UK ship support contract), and Spearfish and Sting Ray torpedoes in service with the Royal Air Force and Royal Navy, respectively.

The governments of the Kingdom of Saudi Arabia and the United Kingdom also agreed detailed arrangements to provide support for Typhoon operations for a three-year period. These arrangements will be operated through a full availability service contract with BAE Systems. Eight Typhoon aircraft were delivered in the year to the Saudi customer under the 2007 Salam production contract.

In July, contracts were agreed by the four European partner nations for 88 Tranche 3A Typhoon aircraft with a contract value to the Group of approximately £2bn. The contracts extend visibility of Typhoon production for the next five years.

BAE Systems is also a significant participant on the US F-35 (Joint Strike Fighter) programme with the combination of both airframe assembly manufacture in the UK and electronic systems supplied from the Group's US operations. The F-35 is expected to progress to high volume production over the coming years.

In October, BAE Systems completed the acquisition of VT Group's 45% shareholding in BVT, creating a wholly-owned subsidiary, BAE Systems Surface Ships Limited. The acquisition followed an agreement with the UK Ministry of Defence in July defining a Terms of Business Agreement setting out a 15-year partnering arrangement, including lead roles for the business on defined surface shipbuilding and support programmes. A significant element of the workload underpinned by this agreement is the manufacture of the Royal Navy's new class of two 65,000 tonne aircraft carriers. Following award of manufacturing contracts, steel cutting commenced in July, marking the start of build of the first of class. The Royal Navy also saw Astute, the first of a new class of nuclear powered attack submarines, commence sea trials in November.

BAE Systems identifies unmanned systems as an increasing priority amongst its customers, driven by rapidly evolving requirements often to meet urgent operational needs. BAE Systems is developing a range of unmanned system solutions to meet those requirements.

In the UK, the Group is developing three unmanned air platforms. A small high endurance air system, Herti, has been operationally deployed. A large twin-engined air platform, Mantis, commenced flight trials in October just 19 months after conception. A third development platform, Taranis, a stealthy unmanned combat air system, is in-build.

People and Total Performance
BAE Systems is dependent on the skills and capabilities of its people. The Group sets high standards for the training and development of employees, and is a major employer of apprentices and graduates. The Group maintains robust processes for career development including succession planning for its senior executives.

Programme execution is an important and easily recognisable embodiment of performance but, in addition, we target an integrated approach to performance, embracing all aspects of our corporate existence. The Group wants to be recognised as a company committed to developing a culture of Total Performance. Successfully embedding this approach will be a key differentiator for the Group. Total Performance focuses not just on what we do but also how we do it. It is about every aspect of the way we do business; Customer Focus, Financial Performance, Programme Execution and Responsible Behaviour. Delivery of the Group's Corporate Responsibility agenda is an essential part of embedding a Total Performance culture across the Group.

Our focus on safety remains a top priority. The tragic loss of Nimrod XV230 over Afghanistan in 2006 and the subsequent Haddon-Cave report published in October have only strengthened our resolve to continuously seek improvements to safety across all aspects of our business. The Product Safety Review we recently announced, headed by Nigel Whitehead, Group Managing Director, Programmes & Support, further demonstrates the importance we place on safety. We will work with our customer, the UK Ministry of Defence, to ensure that any learning benefits our current and future workload.

We are also deeply saddened to report the death of one of our employees during deployment of communications equipment in Australia. We are reviewing the cause of this accident and co-operating fully with the regulatory investigation.

BAE Systems aims to achieve leadership standards of responsible business conduct through its programme to address the 23 recommendations of the Woolf Report. As a consequence, we reviewed all Group policies and governance processes during 2009, and have incorporated appropriate changes in the Operational Framework effective January 2010. A further key focus during 2009 was the rolling-out of a Group-wide Code of Conduct for employees as part of the drive to embed high standards of business conduct.

In addition, we have also launched Responsible Trading Principles. All trading is to be undertaken in accordance with these principles and consistency of this approach is key in defining BAE Systems' reputation. Together with our global Code of Conduct, these underpin the way we do business.

BAE Systems is not complacent and recognises the difficulties in the wider economies in which it operates, but it is a broadly-based and robust business with a large order book. It has been agile in developing the business, adapting its capabilities in anticipation of changing requirements.

The result is a continuously evolving business with a good track record of identifying and exploiting growth opportunities whilst re-focusing the business towards the future priority needs of our customers.

PRELIMINARY RESULTS STATEMENT *CONTINUED*

Summary income statement

	2009 £m	2008 £m
Sales[1]	**22,415**	18,543
Underlying EBITA[2]	**2,220**	1,897
Profit on disposal of businesses	**68**	238
Pension accounting gain	**261**	–
Regulatory penalties	**(278)**	–
EBITA	**2,271**	2,135
Amortisation of intangible assets	**(286)**	(247)
Impairment of intangible assets	**(973)**	(177)
Net financial (expense)/income[1]	**(707)**	697
Taxation expense[1]	**(350)**	(640)
(Loss)/profit for the year	**(45)**	1,768
Basic (loss)/earnings per share	**(1.9)p**	49.6p
Underlying earnings[3] per share	**40.7p**	37.1p
Dividend per share	**16.0p**	14.5p

Exchange rates

	2009	2008
£/$ – average	**1.566**	1.853
£/$ – year end	**1.615**	1.451
£/€ – average	**1.123**	1.258
£/€ – year end	**1.125**	1.042

Segmental analysis

	Sales[1]		Underlying EBITA[2]	
	2009 £m	2008 £m	**2009 £m**	2008 £m
Electronics, Intelligence & Support	**5,637**	4,459	**575**	506
Land & Armaments	**6,738**	6,407	**604**	566
Programmes & Support	**6,298**	4,638	**670**	491
International	**4,253**	3,333	**442**	435
HQ & Other Businesses	**254**	235	**(71)**	(101)
Intra-group	**(765)**	(529)	**–**	–
	22,415	18,543	**2,220**	1,897

Order book[1] increased to £46.9bn (2008 £46.5bn) largely reflecting the acquisition of VT Group's 45% interest in the BVT Surface Fleet (BVT) joint venture (£2.1bn). Excluding the impact of exchange translation, the order book is broadly unchanged year-on-year.

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 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 Group's balance sheet.

Sales[1] increased by 21% to £22.4bn (2008 £18.5bn). Like-for-like growth, after adjusting for the impact of exchange translation, and acquisitions and disposals, was 7%. Despite the planned lower level of land vehicle sales in the US, growth was delivered through increased deliveries of Typhoon Tranche 2 standard aircraft to the European partner nations, initial deliveries of Typhoon aircraft and support to the Kingdom of Saudi Arabia, and a 6% underlying growth in the Electronics, Intelligence & Support operating group. US-led businesses were responsible for 55% (2008 59%) of sales[1]. 91% of sales[1] were generated from home markets (2008 88%).

Underlying EBITA Management uses an underlying profit measure to monitor the year-on-year profitability of the Group, which is defined as earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items. This definition is referred to as Underlying EBITA. In order to ensure that it continues to provide a measure of profitability that is comparable over time, it has been amended to exclude all non-recurring items. Underlying EBITA continues to be the measure of profit on which segmental performance is monitored by management. As such, it is disclosed in note 2 on a segmental basis.

Underlying EBITA[2] increased by 17% to £2,220m (2008 £1,897m). This includes favourable exchange translation of £187m. Return on sales reduced to 9.9% after expensing of the Mine Resistant Ambush Protected (MRAP) All-Terrain Vehicles (ATV) research and development, and bid costs (£56m) in the US businesses, and for trading initial deliveries of Typhoon to the Kingdom of Saudi Arabia at lower margins reflecting the early stage of that contract. US-led businesses delivered 53% (2008 57%) of the Group's underlying EBITA[2].

Non-recurring items are defined as items that are relevant to an understanding of the Group's performance with reference to their materiality, nature and function. The non-recurring items for the current and prior years are as follows:

Profit on disposal of businesses comprised the finalisation of the accounting gain recognised in 2008 on the disposal of the Group's interests in the businesses contributed to the BVT joint venture following acquisition of VT Group's 45% interest in 2009 (£58m) and additional proceeds received in respect of the disposal in 2008 of the Group's interest in Flagship Training (£10m). The prior year profit of £238m included the accounting gain on the disposal of the Group's interests in the businesses contributed to BVT (£121m), and profit on disposals of the Surveillance & Attack business (£61m) and the Group's interest in Flagship Training (£56m).

The **pension accounting gain** of £261m in 2009 has resulted from pension benefit restructuring in the US. It has been excluded from underlying EBITA[2] on the basis of its materiality and non-recurring nature.

The **regulatory penalties** of £278m in 2009 reflect the global settlement of the regulatory investigations by the US Department of Justice and the UK's Serious Fraud Office. These have been excluded from underlying EBITA[2] on the basis of their materiality and non-recurring nature.

Amortisation of intangible assets is £39m higher at £286m mainly for the impact of a full year of charges in respect of the businesses acquired in 2008.

Impairment of intangible assets of £973m primarily relates to the goodwill and intangible assets acquired with Armor Holdings in 2007. The impairment largely reflects the non-award of the follow-on Family of Medium Tactical Vehicles production contract (£592m) and the weaker outlook for the US-based Products Group business (£264m). In addition, £34m has been taken relating to the discontinued financial services element of the Detica business. The prior year charge of £177m included a reduction in the market value of the Group's interest in Saab of Sweden (£120m) and a charge against the Products Group (£40m).

Net financial expense[1] was £707m (2008 net financial income £697m). The underlying net interest charge increased to £195m (2008 £102m) primarily on the cash cost of business acquisitions made in 2008, lower interest received on cash held and the carrying cost of $1.5bn US bonds issued in June 2009. A net expense of £512m (2008 net credit £799m) arose from pension accounting, marked-to-market revaluation of financial instruments and foreign currency movements, reversing much of the net income recorded in 2008 from these items.

Taxation expense[1] reflects an effective tax rate of 28% (2008 26%), which is expected to increase to 29% in 2010. The effective tax rate is based on profit before taxation excluding goodwill impairment of £725m and regulatory penalties (£278m).

Basic loss per share, in accordance with IAS 33, *Earnings per Share*, was 1.9p (2008 earnings 49.6p). The reduction on 2008 mainly reflects the impairments, regulatory penalties, and reversal of gains made in 2008 on marked-to-market revaluation of financial instruments and foreign currency movements.

Underlying earnings[3] **per share** was 40.7p (2008 37.1p), an increase of 10%.

Dividends The Board is recommending a final dividend of 9.6p per share (2008 8.7p), bringing the total dividend for the year to 16.0p per share (2008 14.5p), an increase of 10%.

The proposed dividend is covered 2.5 times by underlying earnings[3] (2008 2.6 times), which is consistent with the Group's policy of growing the dividend whilst maintaining a long-term sustainable earnings cover of approximately two times.

Reconciliation of cash inflow from operating activities to net cash

	2009 £m	2008 £m
Cash inflow from operating activities	**2,232**	2,009
Capital expenditure (net) and financial investment	**(489)**	(503)
Dividends received from equity accounted investments	**77**	89
Assets contributed to Trust	**(225)**	–
Operating business cash flow	**1,595**	1,595
Interest	**(186)**	(98)
Taxation	**(350)**	(261)
Free cash flow	**1,059**	1,236
Acquisitions and disposals	**(253)**	(1,001)
Debt acquired on acquisition of subsidiary	**(1)**	(37)
Purchase of equity shares (net)	**(20)**	(27)
Equity dividends paid	**(534)**	(478)
Dividends paid to minority interests	**(5)**	(11)
Cash inflow/(outflow) from matured derivative financial instruments	**36**	(440)
Movement in cash collateral	**(11)**	106
Movement in cash received on customers' account[4]	**(12)**	26
Foreign exchange	**262**	(374)
Other non-cash movements	**(157)**	339
Movement in net cash as defined by the Group	**364**	(661)
Opening net cash as defined by the Group	**39**	700
Closing net cash as defined by the Group	**403**	39

Components of net cash as defined by the Group

	2009 £m	2008 £m
Debt-related derivative financial assets	**39**	203
Other investments – current	**211**	–
Cash and cash equivalents	**3,693**	2,624
Loans – non-current	**(2,840)**	(2,608)
Loans and overdrafts – current	**(453)**	(173)
Cash received on customers' account[4]	**(20)**	(7)
Assets held in Trust	**(227)**	–
Closing net cash as defined by the Group	**403**	39

Operating business cash flow

	2009 £m	2008 £m
Electronics, Intelligence & Support	**380**	380
Land & Armaments	**480**	467
Programmes & Support	**285**	651
International	**816**	163
HQ & Other Businesses	**(366)**	(66)
Operating business cash flow	**1,595**	1,595

Cash inflow from operating activities was £2,232m (2008 £2,009m), which includes contributions in excess of service costs for the UK and US pension schemes totalling £475m (2008 £321m).

There was an outflow from **net capital expenditure and financial investment** of £489m (2008 £503m), which included £94m (2008 £183m) in respect of new residential and office facilities in Saudi Arabia.

Dividends received from equity accounted investments, primarily MBDA, Saab and Eurofighter, totalled £77m (2008 £89m).

Assets contributed to Trust comprises the £225m of payments made into Trust during the year for the benefit of the Group's main pension scheme. As the use of these assets is restricted under the terms of the Trust, they are excluded from the Group's definition of net cash. Consistent with the presentation of other one-off contributions into the Group's pension schemes, the contribution is presented within operating business cash flow.

Interest increased to £186m (2008 £98m) largely reflecting the cash cost of business acquisitions in 2008, lower interest received on the Group's cash holdings and the carrying cost of the $1.5bn US bonds issued in June 2009.

Taxation payments increased to £350m (2008 £261m) mainly as a result of the higher taxable profits generated by the Group in 2008.

Net cash outflow in respect of **acquisitions and disposals** was £253m. This mainly comprises net payments made to acquire VT Group's 45% interest in BVT, including acquired cash (£315m), and Advanced Ceramics Research, Inc. (£9m), less the deferred consideration received relating to the 2008 disposal of a 50% interest in Flagship Training (£70m). In the prior year, the Group acquired MTC, Tenix Defence and Detica, and disposed of the Surveillance & Attack business and interest in Flagship Training for net cash consideration of £1bn.

The Group finances part of its investment in its US businesses through an intercompany loan. As at 31 December 2009, $2.1bn (2008 $2.1bn) of a total of $3.6bn (2008 $6.6bn) was hedged using a rolling programme of short-term foreign exchange hedges. As a consequence of the weakening of the US dollar, there has been a **cash inflow from matured derivative financial instruments** of £36m (2008 outflow £440m) from rolling these hedges into 2010.

Foreign exchange translation during the year, primarily in respect of the Group's US dollar-denominated borrowing, increased reported cash by £262m.

Share repurchase programme
In 2010, the Group will initiate a programme to return up to £500m to shareholders by way of a market purchase of shares. This programme is set in the context of an appropriately balanced use of capital. In addition to this accelerated return to shareholders, the Group will continue to pursue its strategy of organic investment and investing in attractive sectors of the defence market through selective acquisitions.

ELECTRONICS, INTELLIGENCE & SUPPORT

The Electronics, Intelligence & Support operating group, with 32,000 employees[1] and headquartered in the US, designs, develops, produces and services systems and subsystems for a wide range of military and commercial applications.

Financial highlights

- Like-for-like organic sales[1] growth of 6% over 2008
- Underlying EBITA[2] excludes a non-recurring accounting gain of £202m from the restructuring of the US pension schemes

Performance

	2009	2008	2007
Sales[1]	**£5,637m**	£4,459m	£3,916m
Underlying EBITA[2]	**£575m**	£506m	£437m
Return on sales	**10.2%**	11.3%	11.2%
Cash inflow[3]	**£380m**	£380m	£302m
Order intake[1]	**£5,416m**	£4,904m	£4,178m
Order book[1]	**£4.5bn**	£5.2bn	£3.5bn

Key points

- Maintained leadership position in electronic warfare systems
- Introduced new infrared technology solutions to improve the effectiveness of US Army troops
- Secured seven-year managed IT services contract for the US Treasury
- Expanded leadership position in hybrid electric propulsion for urban mass transit buses
- Selected to provide US military counter-insurgency support services under a five-year urgent-needs contract

Looking forward

BAE Systems remains focused on winning strategic contracts in information technology, cyber, mission support and services. The business continues to capitalise on its leadership positions in electronic warfare and infrared technologies, and expand its diverse mix of commercial and civil government businesses in areas such as ship repair, information technology and commercial aviation. It also continues to invest in the growing fields of energy management, Readiness & Sustainment services and cybersecurity.

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 4).
3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments and assets contributed to Trust.

In 2009, Electronics, Intelligence & Support (EI&S) achieved sales[1] of £5,637m (2008 £4,459m). On a like-for-like basis, sales[1] growth was 6% over 2008.

Underlying EBITA[2] of £575m (2008 £506m) excludes a non-recurring accounting gain of £202m from the restructuring of the US pension schemes. Return on sales reduced to 10.2% (2008 11.3%). In 2008, there was a credit of £23m from share scheme mark-to-market accounting.

Operating cash inflow[3] was £380m (2008 £380m).

Electronic Solutions
Electronic Solutions continued to demonstrate its leadership position in the electronic warfare market through Low-Rate Initial Production (LRIP) awards for electronic warfare suites on the F-35 Lightning II. During 2009, orders totalled more than $220m (£136m). Deliveries on the first four LRIP contracts will conclude in 2012, and future contract awards are anticipated to support aircraft deliveries to the US government and international partner countries.

US Army demand for thermal weapon sights drove deliveries of some 36,000 systems valued at $340m (£217m) in 2009 under the five-year Indefinite-Delivery/Indefinite-Quantity (IDIQ) contract. Cumulative orders for these weapon sights exceed $500m (£310m) for 68,000 sights.

US Army orders for the Common Missile Warning Systems (CMWS) totalled more than $100m (£62m) in 2009. CMWS is a helicopter missile warning system that detects incoming missiles, rejects false alarms, and cues the onboard infrared jamming system to the missile’s location. The system logged its millionth combat flight hour during the year.

Two IDIQ contracts were received from the US Army for the Laser Target Locator Module and the Driver’s Vision Enhancer Family of Systems. The lightweight target locators enable soldiers to quickly, safely and accurately determine target coordinates in daylight or darkness, and the vision enhancement systems provide all-weather, day/night visibility to operators of combat and logistics vehicles. Initial orders for the two systems totalled $115m (£71m) in 2009.

The US Navy selected a BAE Systems-Alliant Techsystems team for the Joint and Allied Threat Awareness System (JATAS) technology demonstration. JATAS is the next-generation missile warning system to protect US Navy and Marine Corps helicopters and tilt-wing aircraft.

Information Solutions
Some two-thirds of the line of business’s activity is in support of the US intelligence community.

The Information Solutions business also positioned itself among the largest providers of managed information technology services, receiving a seven-year contract to manage Information Technology (IT) operations for the US Treasury, valued at up to $325m (£201m).

The business received a contract for up to $148m (£92m) from the US Department of Homeland Security to support the agency's fingerprint image tracking programme.

In the government intelligence market, Information Solutions emerged as a leader in analysis of full-motion video and other advanced imagery, doubling the number of its own imagery analysts, and opening a facility to train analysts for the military and intelligence communities.

BAE Systems' prominent role in the information technology sector was recognised by Computerworld magazine which named the business one of the top 100 IT employers in the US.

Platform Solutions
Platform Solutions further expanded its leadership in hybrid propulsion for urban mass transit. The HybriDrive® propulsion system made its European debut, demonstrated on vehicles in partnership with UK-based manufacturer, Alexander Dennis Limited. As part of a Transport for London trial programme, BAE Systems has hybrid propulsion systems for 12 double-deck and five single-deck buses.

The business is well positioned for a hybrid bus production order for London's transit fleet in 2010. The efficient, emissions-reducing hybrid technology now powers more than 2,000 buses in North America and will enter the Seattle transit fleet in 2010 following the award of a contract from Daimler Buses North America which received a 500-unit order (with an option for 200 additional units) from the Seattle Transit Agency.

Following the US Army's development of the Common Modular Power System as its standard power management architecture for all legacy and modern vehicles, the business received its first production contract in support of the Paladin self-propelled howitzer.

Platform Solutions received the launch order for its holographic pilot display technology. The UK Ministry of Defence selected the Q-Sight™ helmet-mounted display for its Lynx helicopter programme, a development that positions the business for an expanded role in low-visibility operation of rotary wing aircraft. The technology provides superior optical performance with reduced weight and cost.

Support Solutions
The US military's Human Terrain Teams programme awarded the business a $350m (£217m), five-year contract to support urgent needs for recruitment, development and operational support of counter-insurgency efforts. Human Terrain Teams embed social scientists within combat brigades to help tacticians in field environments understand local cultures.

A $320m (£198m), five-year US Army contract was received to provide counter-Improvised Explosive Device (IED) operations and mission support covering comprehensive, all-source intelligence analysis to assist in the global counter-IED fight.

The US Navy awarded a $233m (£144m) contract for engineering and other services to support C4ISR (Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance) systems at land-based facilities, and on platforms such as ships, submarines and ground vehicles.

In the Ship Repair business, the US Navy's first ever full ship modernisation was completed, a year-long, $31m (£19m) upgrade of the USS Bunker Hill. The maintenance, repair and modernisation programme was concluded on time and met all critical milestones.

LAND & ARMAMENTS

The Land & Armaments operating group, with 19,800 employees[1] and headquartered in the US designs, develops, produces, supports and upgrades armoured combat vehicles, tactical wheeled vehicles, naval guns, missile launchers, artillery systems, munitions and law enforcement products.

Financial highlights

- Underlying EBITA[2] excludes a non-recurring accounting gain of £59m from the restructuring of the US pension schemes
- Underlying EBITA[2] includes £42m of costs associated with the unsuccessful Mine Resistant Ambush Protected (MRAP) All-Terrain Vehicle (ATV) bid that were expensed in the year
- Impairment charges of £927m mainly on the Family of Medium Tactical Vehicles (FMTV) programme and Products Group business

Performance

	2009	2008	2007
Sales[1]	**£6,738m**	£6,407m	£3,538m
Underlying EBITA[2]	**£604m**	£566m	£324m
Return on sales	**9.0%**	8.8%	9.2%
Cash inflow[3]	**£480m**	£467m	£10m
Order intake[1]	**£3,934m**	£8,568m	£4,535m
Order book[1]	**£7.8bn**	£11.5bn	£7.3bn

Key points

- Organisation realigned with global strategy
- High volume of vehicle reset and support activity
- Improving performance through rationalisation and efficiencies
- Loss of follow-on production contract for FMTV

Looking forward

In the near term, Land & Armaments will be operating in an increasingly challenging market, brought about by shifting national priorities and pressure on defence budgets, particularly in our US and UK markets. The rest of world market is expected to provide export opportunities over the same period. The business is being shaped to perform in these market conditions through an ongoing drive for rationalisation and efficiency.

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In 2009, Land & Armaments achieved sales[1] of £6,738m (2008 £6,407m). On a like-for-like basis, sales were 8% below 2008 reflecting the lower level of land vehicle sales, primarily on the Mine Resistant Ambush Protected (MRAP) programme, which totalled £0.2bn in 2009 (2008 £1.7bn).

Underlying EBITA[2] was £604m (2008 £566m), which excludes a non-recurring accounting gain of £59m from the restructuring of the US pension schemes. Excluding costs of £42m associated with the unsuccessful MRAP All-Terrain Vehicle (ATV) bid that were expensed in the year, return on sales increased to 9.6% (2008 8.8%).

Operating cash inflow[3] was £480m (2008 £467m).

Order intake[1] was £3,934m (2008 £8,568m). Intake in 2008 included significant awards for the 15-year UK munitions capability contract and Family of Medium Tactical Vehicles (FMTV).

United States

BAE Systems continued in its role as a premier combat systems supplier to the US Army Heavy Brigade Combat Team (HBCT), providing remanufacturing, reset and support for key brigade components. BAE Systems was awarded $791m (£490m) of contracts for Bradley Fighting Vehicles and $277m (£172m) of contracts for Hercules M88 Recovery Vehicles during 2009 while delivering more than 1,500 completed vehicles to the customer.

The business was awarded an initial $64m (£40m) Paladin Integrated Management contract to modernise the M109A6 Paladin self-propelled howitzer system, including the design, fabrication and testing of five prototypes and two support vehicles.

BAE Systems continued to build the FMTV trucks with contracts for approximately $2bn (£1.2bn) per year to the end of 2010. Some 8,400 trucks were manufactured and delivered to the US Army in 2009.

A setback for the Group was the notification by the US Department of Defense in August 2009 and, following a re-evaluation of the bids, in February 2010 that a follow-on production contract for vehicles under the FMTV programme had been lost.

A new Euro V-compliant Global Tactical Vehicle has been designed and produced to address European market requirements. The vehicle was unveiled at the biennial Defence Systems & Equipment international exhibition in the UK in September.

The personnel security business secured over $371m (£230m) of contracts for individual soldier protection, with contracts for Modular Lightweight Load Carrying Equipment from the Defense Logistics Agency as well as contracts for over 230,000 Outer Tactical Vests.

As part of the ongoing realignment of the Land & Armaments business in the US, the business has implemented rationalisation programmes reducing headcount by 12% and the closure of seven facilities.

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 4).
3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments and assets contributed to Trust.

United Kingdom

Under the 15-year munitions partnering agreement with the UK Ministry of Defence (MoD), delivery rates on small arms ammunition continued at an average of one million rounds per day in support of current operations. As committed under the agreement, £15m has been invested so far in new manufacturing operations out of the total programme for more than £120m.

Significant work is underway to support operations in Afghanistan, particularly in carrying out urgent operational upgrade work to vehicles such as the Warrior and the new Panther, to continue to protect against rapidly evolving threats.

The business submitted competitive bids into both the Future Rapid Effects System (FRES) Specialist Vehicle (SV) and Warrior upgrade programmes, the outcomes of which are currently expected to be known in 2010.

The BAE Systems turret design is optimised for the new cased-telescoped ammunition weapon system, the CT40, which was mandated by the UK MoD for both the Warrior and FRES SV programmes.

With a new schedule on the Terrier armoured tractor programme agreed at the end of 2008, the MoD confirmed the production of 60 vehicles with enhancements to improve protection beyond the original design. Production began in early 2010.

The business received new orders for the production and support of the M777 155mm lightweight howitzer, for both the US and Canadian armed forces. A total of 158 M777s were delivered in 2009. The M777 system has been deployed on operations in both Afghanistan and Iraq.

As part of its ongoing restructuring, the business announced over 500 job losses and the closure of three sites.

Sweden

Contracts for 24 BvS10 Viking amphibious all-terrain vehicles were awarded by the UK MoD for a value of £16m. All 24 will be of the new up-armoured MkII variant. In December, the BvS10 was selected following a competition to supply vehicles to the French armed forces and a contract for up to €220m (£196m) was awarded.

Export deliveries continued for CV90 vehicles and support to several customers around the world, including the Netherlands, Denmark and Sweden.

The 155mm Archer self-propelled artillery system has been selected and confirmed by both Sweden and Norway with contracts for a total of 48 systems expected to be signed in early 2010.

A successful legal appeal was made against the decision of the Swedish Defence Materiel Administration (FMV) in June 2009 to choose a competitor’s vehicle for the Armoured Wheeled Vehicle programme. The Administrative Court of Stockholm ruled in October that the FMV must re-compete the procurement. The outcome of the competition is currently expected in 2010.

The Swedish businesses have announced job losses in 2009, totalling approximately 350, as a consequence of restructuring activity.

South Africa

The South African business continued to deliver RG vehicles to several customers around the world, including completing the delivery of RG32M vehicles to Sweden, RG31 vehicles to Spain and RG31 MRAP vehicles to the US.

Building on the success of the RG range of vehicles, a new vehicle, the RG35, has been designed and built. The RG35 is a 6x6 mine protected multi-purpose fighting vehicle and was launched to the market in September.

PROGRAMMES & SUPPORT

The Programmes & Support operating group, with 33,200 employees[1], primarily comprises the Group's UK-based air, naval and security activities.

Financial highlights

- Sales[1] increased over 2008 on commencement of aircraft deliveries and support on the Saudi Typhoon programme, increased deliveries of the Typhoon Tranche 2 standard, and a full year of Detica sales
- Underlying EBITA[2] increased by 36%
- £8.8bn of orders[1] booked in the year, increasing order book[1] to £24.3bn

Performance

	2009	2008	2007
Sales[1]	**£6,298m**	£4,638m	£5,327m
Underlying EBITA[2]	**£670m**	£491m	£456m
Return on sales	**10.6%**	10.6%	8.6%
Cash inflow[3]	**£285m**	£651m	£807m
Order intake[1]	**£8,789m**	£4,195m	£9,091m
Order book[1]	**£24.3bn**	£19.8bn	£20.9bn

Key points

- Typhoon Tranche 3A secured
- Over £3bn of support orders received
- Astute submarine commenced sea trials
- Second Type 45 accepted off contract
- Acquisition of VT Group plc's 45% interest in the BVT joint venture, now 100% owned and re-named BAE Systems Surface Ships
- Detica security business performing strongly in the first full year since acquisition
- Continued rationalisation activity

Looking forward

Programmes & Support is driven by its existing strong order book, and the level of future UK Ministry of Defence (MoD) funding to meet current UK armed forces operational requirements and delivery of the Defence Industrial Strategy. A Strategic Defence Review will begin after the general election in 2010.

In Military Air Solutions, growth is linked to increased combat aircraft production activity and in-service support performance.

Surface Ships is underpinned by the six-ship Type 45 destroyer programme, the manufacturing phase of the Queen Elizabeth Class carrier programme, export contracts and the 15-year Terms of Business Agreement with the UK MoD.

The Submarine Solutions business remains focused on the Astute programme, and on delivering the concept design work for the Successor Programme. Follow-on orders for Astute are key to retaining the skill base necessary to design and build a next-generation nuclear deterrent submarine.

Detica's reputation in the UK security market, repositioning to become a solution integrator and the publication of the UK government cybersecurity strategy, mean the business is positioned to benefit from continued government focus on intelligence, security and resilience.

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 4).
3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments and assets contributed to Trust.

Sales[1] in 2009 were £6,298m (2008 £4,638m). Sales[1] growth was 36% largely due to the commencement of aircraft deliveries and support on the Saudi Typhoon programme, increased deliveries of the Typhoon Tranche 2 standard, and a full year of Detica sales.

Underlying EBITA[2] was £670m (2008 £491m) with return on sales maintained at 10.6%.

Operating cash inflow[3] was £285m (2008 £651m) reflecting the utilisation of programme advance funding.

Order intake[1] increased by £4.6bn to £8,789m (2008 £4,195m), giving a closing order book[1] of £24.3bn.

Military Air Solutions

In 2009, the business secured contracts totalling almost £3bn for availability support on the Typhoon and Harrier aircraft fleets, and the Typhoon Tranche 3A production contract for 88 aircraft.

Delivery of Typhoon aircraft to the four partner nations and Austria continues with 208 aircraft delivered, 50 being Tranche 2 standard aircraft. The first eight of 72 Typhoons were delivered to the Royal Saudi Air Force. Upgrade work on the Tranche 1 aircraft continues to provide the UK Royal Air Force (RAF) with increased operational capability.

In March, the UK government awarded the business a £430m five-year Typhoon Availability Service (TAS) contract to work with the RAF to ensure aircraft are available to meet operational commitments. In September, the Typhoon Support Centre and Maintenance Facility were officially opened at RAF Coningsby, marking the official start of our TAS undertaking.

A five-year contract worth in excess of £400m to provide a support service for the Radar and Defensive Aids Sub-System (DASS) for the Typhoon fleets of the air forces of the UK, Germany, Italy and Spain was awarded in October.

On the Tornado and Harrier programmes, operational requirements continued to be met through both the delivery of contractual milestones and Urgent Operational Requirements to support aircraft in theatre.

The UK MoD also awarded the Harrier Platform Availability Contract worth in excess of £550m to support the UK's Joint Force Harrier Fleet until their planned out of service date.

During the year, six Gripen aircraft were accepted by the South African customer. Hawk aircraft deliveries for South Africa are now complete and the programme is in the support phase.

Aircraft acceptances of the Hawk Mk128 Advanced Jet Trainer for the RAF are progressing, with 17 of 28 now accepted. Activity under the Hawk Integrated Operational Support programme continues, with aircraft availability consistently in excess of the 95% target.

Support continues to Hindustan Aeronautics Limited of India to conclude negotiations on the requirement for a further 57 Hawks in India.

The first production Nimrod MRA4 made a successful maiden flight from Woodford in September. Formal customer acceptance is anticipated in early 2010.

On F-35 Lightning II, major airframe units and systems for all three aircraft variants under development and initial production contracts have been delivered. The first F-35 airframes are in the UK for structural testing and the UK government has committed to order three of the Short Take Off and Vertical Landing (STOVL) aircraft for operational test and evaluation.

BAE Systems continues to leverage its expertise and capabilities in Unmanned Aircraft Systems and position itself in this growth market with Mantis making its first flight in October. Good progress is being made on Herti, with ongoing flight trials of the production standard variant. Final assembly of the Taranis advanced technology demonstrator is underway.

In September, consultations started on a programme of approximately 1,100 potential job losses across UK sites at Woodford, Samlesbury, Warton and Farnborough.

Following the publication of the independent report by Charles Haddon-Cave QC into the loss of Nimrod XV230 over Afghanistan in 2006, BAE Systems has appointed Dr Chris Elliott FREng, a leading systems engineer and barrister, to support and advise Nigel Whitehead FREng, Group Managing Director, Programmes & Support, who will undertake a review of the Group's approach to product safety across all its sectors in the UK.

BAE Systems Surface Ships
In October, the Group acquired VT Group plc's 45% shareholding in BVT Surface Fleet Limited. The wholly-owned subsidiary has been re-named BAE Systems Surface Ships Limited.

In July 2009, the business signed a 15-year Terms of Business Agreement with the UK MoD, providing a minimum of 15 years exclusivity for the design, build and integration on specified MoD shipbuilding programmes, including the Future Surface Combatant. It also gives a contractual guarantee to deliver a minimum of £350m of financial benefits to the MoD over the duration of the contract.

On the Type 45 programme, the second ship, Dauntless, was accepted off contract in Portsmouth in December. The third ship, Diamond, has completed her first sea trials and the fifth ship, Defender, was launched in October. In September, a multi-year contract for over £300m was signed for the in-service support of the six Type 45 destroyers.

Under the Queen Elizabeth Class aircraft carriers programme, a revised build strategy was announced in March under which BAE Systems, as part of the Aircraft Carrier Alliance, will deliver substantial sections from the Clyde and Portsmouth shipyards, as well as managing the integration of the ships at Rosyth. First steel was cut in July, engineering works to facilitate the delivery of the blocks from the Govan yard have been completed and substantial progress has been made in fabrication of units for the first ship, HMS Queen Elizabeth.

On export programmes, the first Oman vessel was launched in June, and the first and second ships for Trinidad & Tobago were launched in August and November, respectively.

Surface Ships continues to support the Royal Navy as its long-term partner in the management of Portsmouth Naval Base.

Submarine Solutions
The first of class Astute submarine successfully completed its nuclear power plant testing programme and has commenced sea trials. This is the first time since the Vanguard Class boats were successfully accepted in 1999 that a new to service submarine has undertaken sea trials in the UK. Ambush, the second Astute boat, is scheduled for launch at the end of 2010.

Involvement in the concept phase for the successor to the Vanguard Class submarine has been extended into 2010 in support of requirements definition.

Detica
Detica has continued to focus on helping its clients to collect, manage and exploit information to reveal actionable information intelligence. Detica is now developing a range of new, innovative technologies for analytical decision support, real-time situational awareness and control, and secure computing and communications. Detica is investing in combining these technologies with its in-depth security and industry knowledge to create differentiated solutions to tackle management of personnel security, defending against chemical, biological, radiological, and nuclear threats and protecting deployed forces.

In the UK market, Detica is repositioning as a solution integrator, combining its core consultancy, specialist products and applications development capabilities to deliver larger-scale systems integration and managed services programmes across both government and commercial markets. A system using Detica NetReveal® has helped Her Majesty's Revenue and Customs to identify and target tax evasion using advanced data analytics. Detica was part of a consortium selected by the Highways Agency to provide consultancy services to the National Road Telecommunications System, as part of a ten-year, £20m programme.

Detica is helping to build international opportunities in the three global security mission areas of cybersecurity, border and transportation security, and counter terrorism and organised crime. The Detica NetReveal® solution also continues to show strong global sales growth, with significant wins during the year. Also during the year, the Reveal suite of software-based solutions has been extended to include TxtReveal™, for analysing large volumes of unstructured data.

Integrated System Technologies (Insyte)
In July, the Seawolf Mid-Life Update system was declared 'In Service' on the Type 23 frigates whilst the update programme continues on the first of class Type 22 frigate.

In November, the FALCON mobile battlefield communication system for the UK Army and RAF passed its Equipment Acceptance Trial.

During the year, the 500th Sting Ray lightweight torpedo was delivered to the UK MoD. A £99m export contract for the Norwegian Navy was secured. In July, the UK MoD placed a ten-year, £370m Torpedo Capability Contract.

Both of the contracted Type 102 Commander air defence radars have now been accepted by the UK MoD and the first system deployed at its operational base.

A revised delivery schedule has been agreed with the UK MoD on the ARTISAN 3D Medium-Range Radar naval programme.

Milestones on the Maritime Composite Training System for use at HMS Collingwood are not being achieved on schedule. A review of the remaining programme is being undertaken to agree a revised delivery schedule.

Following a review of forward workload, the business announced a redundancy programme in November involving a loss of up to 642 jobs.

INTERNATIONAL

The International operating group, with 19,700 employees[1], comprises the Group's businesses in Saudi Arabia and Australia, together with a 37.5% interest in the pan-European MBDA joint venture, a 20.5% shareholding in Saab of Sweden and a 49% shareholding in Air Astana.

Financial highlights

- Like-for-like sales[1] growth of 15% over 2008
- Good operating cash flow[3] performance

Performance

	2009	2008	2007
Sales[1]	**£4,253m**	£3,333m	£3,359m
Underlying EBITA[2]	**£442m**	£435m	£435m
Return on sales	**10.4%**	13.1%	13.0%
Cash inflow[3]	**£816m**	£163m	£678m
Order intake[1]	**£4,825m**	£4,065m	£3,876m
Order book[1]	**£11.6bn**	£11.0bn	£7.9bn

Key points

- Entry into service of Typhoon aircraft under the Salam programme
- Order intake[1] secured for three-year support to Typhoon aircraft for the Kingdom of Saudi Arabia
- Order award for Australian Air Warfare Destroyer build programme
- Delivery of four inshore patrol vessels to New Zealand MoD

Looking forward

The Group seeks to sustain its long-term presence in the Kingdom of Saudi Arabia through delivering on current programmes and industrialisation commitments, and developing new business, including in the land sector.

In Australia, the Defence White Paper and 2009-10 Budget included a commitment to increased defence funding for the next decade by approximately 3% per annum and a Strategic Reform Programme that will place cross-service pressure on support budgets. BAE Systems is well placed to benefit from both new defence procurement and increased Readiness & Sustainment activities.

During 2009, International achieved sales[1] of £4,253m (2008 £3,333m). The increase in sales[1] was predominantly a result of a full 12 months of trading from the acquired Tenix Defence business and entry into service of Typhoon aircraft in the Kingdom of Saudi Arabia.

Underlying EBITA[2] was £442m (2008 £435m) generating a return on sales of 10.4% (2008 13.1%). The reduction in return on sales is due to the low margin traded in the early stages of the Salam programme and the acquired Tenix Defence business being at lower margins than the average of this operating group.

Operating cash inflow[3] was £816m (2008 £163m).

CS&S International

BAE Systems has a major presence in the Kingdom of Saudi Arabia (KSA). It acts as prime contractor for the UK/KSA government-to-government defence agreement. It also holds certain direct contracts with the Saudi government. Progress is ongoing to modernise the Saudi armed forces in line with the Understanding Document signed in December 2005 between the UK and KSA governments.

Around 4,900 people are employed by the Group in the Kingdom of Saudi Arabia, of whom approximately half are Saudi nationals. The business continues to develop its presence in Saudi Arabia and remains committed to developing a greater indigenous capability in the Kingdom. This is being enhanced by the entry into service of the Typhoon aircraft and the subsequent development of the Typhoon industrial base in Saudi Arabia.

Of the 72 Typhoon aircraft contracted in 2007 under the Salam programme, eight were delivered in the year to the customer in line with programme. The initial support solution contract was also agreed and flying operations commenced.

The business continues to support the operational capability of both the Royal Saudi Air Force and Royal Saudi Naval Forces. Significant incremental orders totalling £1.2bn were received in the period for the Tornado Sustainment Programme (TSP) weapons contract, Naval Minehunter Mid-Life Update and a multi-year Naval Training Programme.

The C4I[4] programme remains challenging and discussions continue with the aim of agreeing the definition of a solution that meets the customer requirement.

The first Tactica land vehicles were delivered to the Saudi Arabia National Guard in June and deliveries have continued through the second half of the year. A contract for the support of Tactica land vehicles has been secured. Further opportunities are being pursued in support of the Royal Saudi Land Force's programme of capability enhancements and equipment upgrades.

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 4).
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 Command, Control, Communications, Computers and Intelligence.

Australia
The Australian Government's Strategic Reform Programme plans A$20bn (£10bn) in internal savings over the next decade through the delivery of significant efficiencies. The business is engaged with the Australian government and Australian Defence Force (ADF) in developing plans and creating opportunities to deliver these efficiencies.

Significant contract awards in 2009 included a A$94m (£52m) contract to enhance and support the ground segment of the ADF's satellite communications capability, contracts potentially worth up to A$570m (£318m) to provide maintenance and upgrades for the Royal Australian Navy's Seahawk and Australian Army's Black Hawk helicopter fleets and Royal Australian Air Force's F/A 18 Hornet fighter aircraft, and a A$309m (£172m) contract to build 36 hull modules for the Royal Australian Navy's three new Air Warfare Destroyers.

In the year, four inshore patrol vessels were delivered to the New Zealand MoD and two offshore patrol vessels are expected to be delivered in the first quarter of 2010. Warranty claims relating to the supply of the multi-role vessel in 2007 that were subject to mediation have been satisfactorily resolved.

The business is a subcontractor to Boeing on the Wedgetail Airborne Early Warning and Control programme. In the year, the business delivered the majority of the ground subsystem and the air subsystem entered the final acceptance testing phase. The business is working to deliver the Electronic Warfare systems in support of the aircraft integration programme.

The Australian government has issued a revised request for the supply of medium and heavy tactical trucks under its Land 121 programme. The Australian business is partnered with BAE Systems Land & Armaments and Scania, and participated in the vehicle trial and evaluation component of the programme. The results of this component, which will be known in the first half of 2010, will be used to down-select two preferred tenderers with contract award expected in 2011.

The programme to supply two Landing Helicopter Dock ships to the Royal Australian Navy is progressing with numerous milestones achieved, including the laying of the keel for the first ship, and the successful completion of the Whole of Ship Detailed Design Review.

The completion accounting process continues with the former owners of the Tenix Defence business in Australia and an expert has been appointed to determine certain matters in dispute.

MBDA (37.5% interest)
MBDA's performance in 2009 delivered an increasing return on sales on broadly unchanged sales volumes.

Order intake in 2009 was strong and included Scalp Naval production in France, a second year contract extension for the UK Complex Weapons programme, and in export markets, Marte anti-ship missiles to the United Arab Emirates, ground-based vertical launch Mica air defence weapons to a Middle Eastern country, Storm Shadow stand-off missiles, and Exocet anti-ship missiles.

Key domestic deliveries included Mica air-to-air missiles, Taurus stand-off missiles and Seawolf naval air defence missiles. Export deliveries included Aster and Mistral surface-to-air missiles, Storm Shadow stand-off missiles and Exocet anti-ship missiles.

Development programmes continue to progress well, with key milestones being passed on the MEADS air-defence programme, Meteor air-to-air missile programme, all Assessment Phases of UK Complex Weapon Programmes and Scalp Naval stand-off missile programme.

Significant evidence has been gathered out of Sea Viper firing campaigns during the year to support the overall system qualification, but an investigation is currently underway to identify the cause of issues arising during these campaigns as well as establishing a revised plan to support the Type 45 programme.

Saab (20.5% shareholding)
Saab's sales were SEK24.6bn (£2.1bn). Operating income was SEK1.4bn (£115m) producing an operating margin of 5.6%, compared with 0.7% in 2008.

Key orders won during 2009 include a SEK700m (£61m) order within the civil security area, Gripen orders from the Swedish Defence Materiel Administration (FMV) of approximately SEK1bn (£87m) to support operational capacity and future capability studies and a SEK1.5bn (£130m) order from the United Arab Emirates for an airborne surveillance system.

In response to market conditions, Saab announced 670 redundancies across its Dynamics and Commercial Aircraft areas of business during the year.

Defence Land Systems India Private Limited (26% shareholding)
As a further step in our strategy of developing India as a home market, the business entered into a joint venture arrangement with Mahindra & Mahindra Limited to create a new land systems-focused joint venture defence company based in India. The joint venture is expected to be established in the first half of 2010.

HQ & OTHER BUSINESSES

HQ & Other Businesses, with 2,200 employees[1], comprises the regional aircraft asset management and support activities, head office and UK shared services activity, including research centres and property management.

Financial highlights

- Settlement with final insurer achieved, enabling closure of the Group's Financial Risk Insurance Programme
- Regional Aircraft profits of £46m following placement of 44 aircraft and settlement of outstanding commercial items
- Underlying EBITA[2] excludes regulatory penalties of £278m

Performance

	2009	2008	2007
Sales[1]	**£254m**	£235m	£243m
Underlying EBITA[2]	**£(71)m**	£(101)m	£(203)m
Cash (outflow)/inflow[3]	**£(366)m**	£(66)m	£181m
Order intake[1]	**£175m**	£212m	£345m
Order book[1]	**£0.4bn**	£0.4bn	£0.4bn

Looking forward

Market conditions for the commercial aircraft market continue to provide a challenging trading environment due to the impact of the global economic downturn and tightened availability of funding to operators.

In 2009, HQ & Other Businesses reported a loss[2] of £71m (2008 loss[2] £101m) on sales[1] of £254m (2008 £235m).

In 2008, impairment charges of £32m were taken in respect of the spares and support business, and aircraft carrying values within Regional Aircraft.

In 2009, the Regional Aircraft business has recognised underlying EBITA[2] of £46m following favourable settlement of some outstanding commercial items, together with profits on sale of aircraft and lease extension activity.

A charge was taken in 2009 for a long-standing commercial dispute on an overseas defence equipment contract.

Operating cash outflow[3] in 2009 was £366m (2008 £66m). This includes additional contributions in respect of UK pension schemes totalling £310m (2008 £104m).

The commercial aircraft market continues to prove challenging in the global economic downturn. Lease and sale discussions with operators are ongoing with regard to current and future fleet requirements, and marketing activity is focused on both uncontracted idle aircraft and those returning off lease.

Whilst support revenues have reduced due to lower demand for aircraft components, this has been partially offset by increased revenues from engineering and technical support services.

Whilst market conditions have impacted the general level of financing available to airlines globally, the portfolio customer base remains relatively robust and the business continues to closely monitor operator performance against default risk.

The balance sheet carrying value of aircraft in the Regional Aircraft business (£189m) is based on the net present value of forecast future net leasing or disposal income.

In the year, a settlement with the remaining insurer under the Group's Financial Risk Insurance Programme was completed.

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 4).
3 Net cash (outflow)/inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments and assets contributed to Trust.

FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December

	Notes	2009 £m	Total 2009 £m	2008 £m	Total 2008 £m
Continuing operations					
Combined sales of Group and equity accounted investments	2		**22,415**		18,543
Less: share of sales of equity accounted investments	2		**(2,041)**		(1,872)
Revenue	2		**20,374**		16,671
Operating costs			**(20,060)**		(15,386)
Other income			**465**		415
Group operating profit excluding amortisation and impairment of intangible assets		**2,038**		2,003	
Amortisation		**(286)**		(247)	
Impairment		**(973)**		(56)	
Group operating profit			**779**		1,700
Share of results of equity accounted investments excluding finance costs and taxation expense		**233**		132	
Financial (expense)/income of equity accounted investments		**(7)**		44	
Taxation expense of equity accounted investments		**(23)**		(37)	
Share of results of equity accounted investments		**203**		139	
Goodwill impairment in respect of equity accounted investments		**–**		(121)	
Contribution from equity accounted investments			**203**		18
EBITA[1] excluding non-recurring items		**2,220**		1,897	
Profit on disposal of businesses[2]		**68**		238	
Pension curtailment gains[2]		**261**		–	
Regulatory penalties[3]		**(278)**		–	
EBITA[1]		**2,271**		2,135	
Amortisation		**(286)**		(247)	
Impairments		**(973)**		(177)	
Financial (expense)/income of equity accounted investments		**(7)**		44	
Taxation expense of equity accounted investments		**(23)**		(37)	
Operating profit			**982**		1,718
Finance costs	3				
Financial income		**1,573**		3,380	
Financial expense		**(2,273)**		(2,727)	
			(700)		653
Profit before taxation			**282**		2,371
Taxation expense					
UK taxation		**(105)**		(351)	
Overseas taxation		**(222)**		(252)	
			(327)		(603)
(Loss)/profit for the year			**(45)**		1,768
Attributable to:					
BAE Systems shareholders			**(67)**		1,745
Minority interests			**22**		23
			(45)		1,768
(Loss)/earnings per share	4				
Basic (loss)/earnings per share			**(1.9)p**		49.6p
Diluted (loss)/earnings per share			**(1.9)p**		49.5p

1 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense.
2 Included in other income.
3 Included in operating costs.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December

	2009 £m	2008 £m
(Loss)/profit for the year	**(45)**	1,768
Other comprehensive income		
Currency translation on foreign currency net investments:		
Subsidiaries	**(246)**	807
Equity accounted investments	**(56)**	197
Amounts (charged)/credited to hedging reserve	**(393)**	469
Gain on revaluation of step acquisition	**103**	–
Net actuarial losses on defined benefit pension schemes:		
Subsidiaries	**(2,008)**	(1,937)
Equity accounted investments	**(54)**	(60)
Fair value movements on available-for-sale investments	**2**	–
Recycling of cumulative currency translation on disposal	**–**	1
Current tax on items taken directly to equity	**64**	58
Deferred tax on items taken directly to equity:		
Subsidiaries	**562**	425
Equity accounted investments	**16**	17
Total other comprehensive income for the year (net of tax)	**(2,010)**	(23)
Total comprehensive income for the year	**(2,055)**	1,745
Attributable to:		
Equity shareholders	**(2,077)**	1,722
Minority interests	**22**	23
	(2,055)	1,745

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	Minority interests £m	Total equity £m
At 1 January 2009	90	1,238	5,974	(68)	7,234	55	7,289
Total comprehensive income for the year	–	–	(511)	(1,566)	(2,077)	22	(2,055)
Share-based payments	–	–	–	52	52	–	52
Share options:							
Proceeds from shares issued	–	5	–	–	5	–	5
Purchase of own shares	–	–	–	(25)	(25)	–	(25)
Ordinary share dividends	–	–	–	(534)	(534)	(5)	(539)
At 31 December 2009	**90**	**1,243**	**5,463**	**(2,141)**	**4,655**	**72**	**4,727**
At 1 January 2008	90	1,222	4,631	23	5,966	36	6,002
Total comprehensive income for the year	–	–	1,343	379	1,722	23	1,745
Share-based payments	–	–	–	51	51	–	51
Share options:							
Proceeds from shares issued	–	16	–	–	16	–	16
Purchase of own shares	–	–	–	(43)	(43)	–	(43)
Other	–	–	–	–	–	7	7
Ordinary share dividends	–	–	–	(478)	(478)	(11)	(489)
At 31 December 2008	90	1,238	5,974	(68)	7,234	55	7,289

CONSOLIDATED BALANCE SHEET

as at 31 December

	Notes	2009 £m	2008 £m
Non-current assets			
Intangible assets		**11,253**	12,306
Property, plant and equipment		**2,552**	2,446
Investment property		**111**	112
Equity accounted investments		**846**	1,034
Other investments		**6**	6
Other receivables		**201**	162
Other financial assets		**133**	514
Deferred tax assets		**1,517**	1,026
		16,619	17,606
Current assets			
Inventories		**887**	926
Trade and other receivables including amounts due from customers for contract work		**3,764**	3,831
Current tax		**17**	14
Other investments		**211**	–
Other financial assets		**216**	674
Cash and cash equivalents		**3,693**	2,624
		8,788	8,069
Total assets		**25,407**	25,675
Non-current liabilities			
Loans		**(2,840)**	(2,608)
Trade and other payables		**(522)**	(701)
Retirement benefit obligations	5	**(4,679)**	(3,365)
Other financial liabilities		**(261)**	(383)
Deferred tax liabilities		**(8)**	(80)
Provisions		**(377)**	(459)
		(8,687)	(7,596)
Current liabilities			
Loans and overdrafts		**(453)**	(173)
Trade and other payables		**(10,218)**	(9,165)
Other financial liabilities		**(94)**	(362)
Current tax		**(676)**	(704)
Provisions		**(552)**	(386)
		(11,993)	(10,790)
Total liabilities		**(20,680)**	(18,386)
Net assets		**4,727**	7,289
Capital and reserves			
Issued share capital		**90**	90
Share premium		**1,243**	1,238
Other reserves		**5,463**	5,974
Accumulated losses		**(2,141)**	(68)
Total equity attributable to equity holders of the parent		**4,655**	7,234
Minority interests		**72**	55
Total equity		**4,727**	7,289

Approved by the Board on 17 February 2010 and signed on its behalf by:

I G King
Chief Executive

G W Rose
Group Finance Director

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December

	Notes	2009 £m	2008 £m
(Loss)/profit for the year		**(45)**	1,768
Taxation expense		**327**	603
Share of results of equity accounted investments		**(203)**	(139)
Net finance costs		**700**	(653)
Depreciation, amortisation and impairment		**1,600**	755
Gain on disposal of property, plant and equipment		**(17)**	(33)
Gain on disposal of investment property		**–**	(5)
Gain on disposal of businesses		**(68)**	(238)
Cost of equity-settled employee share schemes		**52**	51
Movements in provisions		**52**	(115)
Decrease in liabilities for retirement benefit obligations		**(657)**	(272)
Decrease/(increase) in working capital:			
Inventories		**6**	46
Trade and other receivables		**52**	(5)
Trade and other payables		**433**	246
Cash inflow from operating activities		**2,232**	2,009
Interest paid		**(250)**	(249)
Interest element of finance lease rental payments		**(2)**	(5)
Taxation paid		**(350)**	(261)
Net cash inflow from operating activities		**1,630**	1,494
Dividends received from equity accounted investments		**77**	89
Interest received		**66**	156
Purchases of property, plant and equipment		**(483)**	(520)
Purchases of intangible assets		**(42)**	(32)
Proceeds from sale of property, plant and equipment		**36**	44
Proceeds from sale of investment property		**–**	5
Purchase of subsidiary undertakings	7	**(357)**	(1,078)
Cash and cash equivalents acquired with subsidiary undertakings	7	**33**	2
Purchase of equity accounted investments	7	**(1)**	(12)
Proceeds from sale of subsidiary undertakings	7	**2**	131
Cash and cash equivalents disposed of with subsidiary undertakings		**–**	(60)
Proceeds from sale of equity accounted investments	7	**70**	16
Net proceeds from (purchase)/sale of other deposits/securities		**(209)**	164
Net cash outflow from investing activities		**(808)**	(1,095)
Capital element of finance lease rental payments		**(13)**	(18)
Proceeds from issue of share capital		**5**	16
Purchase of own shares		**(25)**	(43)
Equity dividends paid		**(534)**	(478)
Dividends paid to minority interests		**(5)**	(11)
Cash inflow/(outflow) from matured derivative financial instruments		**36**	(440)
Cash (outflow)/inflow from movement in cash collateral		**(11)**	106
Cash inflow from loans		**920**	–
Cash outflow from repayment of loans		**(133)**	(306)
Net cash inflow/(outflow) from financing activities		**240**	(1,174)
Net increase/(decrease) in cash and cash equivalents		**1,062**	(775)
Cash and cash equivalents at 1 January		**2,605**	3,046
Effect of foreign exchange rate changes on cash and cash equivalents		**11**	334
Cash and cash equivalents at 31 December		**3,678**	2,605
Comprising:			
Cash and cash equivalents		**3,693**	2,624
Overdrafts		**(15)**	(19)
Cash and cash equivalents at 31 December		**3,678**	2,605

NOTES TO THE ACCOUNTS

1. Accounting policies

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

The following interpretations to published standards are effective for accounting periods beginning on or after 1 January 2009:

– IAS 1 (revised 2007), *Presentation of Financial Statements*, requires that the Group present a 'statement of comprehensive income' and a 'consolidated statement of changes in equity' as primary statements. The standard is concerned with disclosure only and has no impact on the reported results or financial position of the Group;

– IAS 23 (revised 2007), *Borrowing Costs*, requires borrowing costs which are directly attributable to the acquisition, construction or production of a qualifying asset (one that takes a substantial period of time to get ready for use or sale) to be capitalised as part of the cost of that asset. This has not had an impact on the reported results or financial position of the Group;

– Amendment to IFRS 2, *Share-based Payment: Vesting Conditions and Cancellations,* provides clarification on the vesting conditions which should be included in the grant date fair value for transactions with employees and others providing similar services. This has had no impact on the reported results or financial position of the Group; and

– *Improvements to IFRSs 2008*, the first standard issued under the International Accounting Standards Board's annual improvement process. It amends 20 existing standards, basis of conclusions and guidance. The improvements include changes in presentation, recognition and measurement requirements and have had no significant impact on the reported results or financial position of the Group.

In addition, the Group has reviewed the effect of the following amendments and interpretations endorsed during 2009 and effective for accounting periods beginning on or after 1 January 2009, and has concluded that they have no impact on the Group's accounts:

– Amendments to IAS 32, *Financial Instruments* and IAS 1, *Presentation of Financial Statements: Puttable Financial Instruments and Obligations Arising on Liquidation*;

– Amendments to IAS 39, *Financial Instruments: Recognition and Measurement* and IFRS 7, *Financial Instruments: Disclosures: Reclassification of Financial Assets*;

– Amendments to IFRS 1, *First-time Adoption of IFRS*, and IAS 27, *Consolidated and Separate Financial Statements: Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*;

– Amendment to IFRS 7, *Financial Instruments – Disclosures*;

– Amendments to International Financial Reporting Interpretations Committee (IFRIC) 9, *Reassessment of Embedded Derivatives* and IAS 39, *Financial instruments: Recognition and measurement: Embedded derivatives*;

– IFRIC 12, *Service Concession Arrangements*;

– IFRIC 13, *Customer Loyalty Programmes*;

– IFRIC 14, IAS 19, *Limit of a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*;

– IFRIC 15, *Agreements for the Construction of Real Estate*; and

– IFRIC 16, *Hedges of a Net Investment in a Foreign Operation*.

Basis of preparation
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

	Combined sales of Group and equity accounted investments		Less: sales by equity accounted investments		Add: sales to equity accounted investments		Revenue	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
Electronics, Intelligence & Support	**5,637**	4,459	**–**	–	**–**	–	**5,637**	4,459
Land & Armaments	**6,738**	6,407	**(6)**	(1)	**–**	1	**6,732**	6,407
Programmes & Support	**6,298**	4,638	**(1,779)**	(1,531)	**1,166**	983	**5,685**	4,090
International	**4,253**	3,333	**(1,513)**	(1,446)	**–**	–	**2,740**	1,887
HQ & Other Businesses	**254**	235	**–**	–	**–**	–	**254**	235
	23,180	19,072	**(3,298)**	(2,978)	**1,166**	984	**21,048**	17,078
Intra-operating group sales/revenue	**(765)**	(529)	**16**	25	**75**	97	**(674)**	(407)
	22,415	18,543	**(3,282)**	(2,953)	**1,241**	1,081	**20,374**	16,671

	Underlying EBITA[1]		Non-recurring items[2]		Amortisation of intangible assets		Impairment of intangible assets		Operating group result	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
Electronics, Intelligence & Support	**575**	506	**202**	61	**(27)**	(24)	**(8)**	–	**742**	543
Land & Armaments	**604**	566	**59**	–	**(177)**	(168)	**(927)**	(40)	**(441)**	358
Programmes & Support	**670**	491	**68**	177	**(49)**	(24)	**(34)**	(5)	**655**	639
International	**442**	435	**–**	–	**(32)**	(30)	**(4)**	(120)	**406**	285
HQ & Other Businesses	**(71)**	(101)	**(278)**	–	**(1)**	(1)	**–**	(12)	**(350)**	(114)
	2,220	1,897	**51**	238	**(286)**	(247)	**(973)**	(177)	**1,012**	1,711
Financial (expense)/income of equity accounted investments									**(7)**	44
Taxation expense of equity accounted investments									**(23)**	(37)
Operating profit									**982**	1,718
Finance costs									**(700)**	653
Profit before taxation									**282**	2,371
Taxation expense									**(327)**	(603)
(Loss)/profit for the year									**(45)**	1,768

1 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
2 Non-recurring items comprise profit on disposal of businesses of £68m (2008 £238m), pension curtailment gains of £261m (2008 £nil) and regulatory penalties of £278m (2008 £nil).

	Assets excluding intangible assets and equity accounted investments		Intangible assets		Equity accounted investments		Total assets		Total liabilities	
	2009 £m	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m	**2009 £m**	2008 £m
Electronics, Intelligence & Support	**1,827**	1,954	**5,082**	5,272	**5**	4	**6,914**	7,230	**(1,366)**	(1,470)
Land & Armaments	**2,030**	2,019	**4,082**	5,712	**(4)**	–	**6,108**	7,731	**(1,482)**	(1,505)
Programmes & Support	**1,485**	866	**1,616**	875	**47**	217	**3,148**	1,958	**(4,611)**	(3,506)
International	**1,622**	1,899	**457**	429	**798**	813	**2,877**	3,141	**(1,921)**	(1,933)
HQ & Other Businesses	**825**	1,690	**16**	18	**–**	–	**841**	1,708	**(2,624)**	(3,035)
	7,789	8,428	**11,253**	12,306	**846**	1,034	**19,888**	21,768	**(12,004)**	(11,449)
Tax							**1,534**	1,040	**(684)**	(784)
Retirement benefit obligations as defined by the Group (note 5)							**42**	40	**(4,452)**	(3,365)
Cash/(debt) as defined by the Group							**3,943**	2,827	**(3,540)**	(2,788)
Consolidated total assets/(liabilities)							**25,407**	25,675	**(20,680)**	(18,386)

NOTES TO THE ACCOUNTS *CONTINUED*

3. Finance costs

	2009 £m	2008 £m
Interest income	**66**	147
Net present value adjustments	**5**	3
Expected return on pension scheme assets	**777**	846
Net gain on remeasurement of financial instruments	**408**	681
Foreign exchange gains	**317**	1,703
Financial income	**1,573**	3,380
Interest expense:		
On bank loans and overdrafts	**(1)**	(2)
On finance leases	**(2)**	(5)
On bonds and other financial instruments	**(225)**	(253)
	(228)	(260)
Facility fees	**(4)**	(4)
Net present value adjustments	**(40)**	(30)
Interest charge on pension scheme liabilities	**(900)**	(795)
Net loss on remeasurement of financial instruments at fair value through profit or loss	**(467)**	(917)
Foreign exchange losses	**(634)**	(721)
Financial expense	**(2,273)**	(2,727)
Net finance costs	**(700)**	653

Additional analysis of finance costs

	2009 £m	2008 £m
Net finance costs – Group	**(700)**	653
Net finance costs – share of equity accounted investments	**(7)**	44
	(707)	697
Analysed as:		
Net interest:		
Interest income	**66**	147
Interest expense	**(228)**	(260)
Facility fees	**(4)**	(4)
Net present value adjustments	**(35)**	(27)
Share of equity accounted investments	**6**	42
	(195)	(102)
Other finance costs:		
Group:		
Net financing (charge)/credit on pensions	**(123)**	51
Market value and foreign exchange movements on financial instruments and investments[1]	**(376)**	746
Share of equity accounted investments	**(13)**	2
	(707)	697

1 The loss in 2009 (2008 gain) primarily reflects net foreign exchange movements on the unhedged portion of an intercompany loan from the UK to the US businesses.

4. Earnings per share

	2009			2008		
	£m	**Basic pence per share**	**Diluted pence per share**	£m	Basic pence per share	Diluted pence per share
(Loss)/profit for the year attributable to equity shareholders	**(67)**	**(1.9)**	**(1.9)**	1,745	49.6	49.5
Add back/(deduct):						
Profit on disposal of businesses, post tax	**(65)**			(208)		
Pension curtailment gains, post tax	**(188)**			–		
Regulatory penalties	**278**			–		
Net financing charge/(credit) on pensions, post tax	**91**			(39)		
Market value movements on derivatives, post tax	**278**			(552)		
Amortisation and impairment of intangible assets, post tax	**384**			184		
Impairment of goodwill – subsidiaries	**725**			54		
Impairment of goodwill – equity accounted investments	**–**			121		
Underlying earnings, post tax	**1,436**	**40.7**	**40.6**	1,305	37.1	37.0

	Millions	**Millions**	Millions	Millions
Weighted average number of shares used in calculating basic earnings per share	**3,532**	**3,532**	3,519	3,519
Incremental shares in respect of employee share schemes		**4**		9
Weighted average number of shares used in calculating diluted earnings per share		**3,536**		3,528

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.

In the 12 months to 31 December 2009, outstanding share options were anti-dilutive and so have been excluded from the diluted loss per share in accordance with IAS 33.

5. Retirement benefit obligations

	UK £m	US and other £m	**Total £m**
Deficit in defined benefit pension plans at 1 January 2009	(3,072)	(1,083)	**(4,155)**
Actual return on assets above expected return	994	264	**1,258**
Increase in liabilities due to changes in assumptions	(3,120)	(222)	**(3,342)**
One-off contributions	85	160	**245**
Recurring contributions in excess of service cost	244	(14)	**230**
Past service cost	(18)	(3)	**(21)**
Curtailment gains	–	261	**261**
Net financing charge	(119)	(26)	**(145)**
Exchange translation	–	96	**96**
Deficit in defined benefit pension plans at 31 December 2009	(5,006)	(567)	**(5,573)**
US healthcare plans	–	(43)	**(43)**
Total IAS 19 deficit	(5,006)	(610)	**(5,616)**
Allocated to equity accounted investments and other participating employers	979	–	**979**
Group's share of IAS 19 deficit excluding Group's share of amounts allocated to equity accounted investments and other participating employers	(4,027)	(610)	**(4,637)**

Represented by:	
Pension prepayments (within trade and other receivables)	**42**
Retirement benefit obligations	**(4,679)**
	(4,637)

Certain of the Group's equity accounted investments participate in the Group's defined benefit plans as well as Airbus SAS, the Group's share of which was disposed of during the year ended 31 December 2006. As these plans are multi-employer plans the Group has allocated an appropriate share of the IAS 19 pension deficit to the equity accounted investments and to Airbus SAS based upon a reasonable and 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 £3,207m (31 December 2008 £2,210m) after tax.

NOTES TO THE ACCOUNTS *CONTINUED*

5. Retirement benefit obligations *continued*

The increase in the liabilities due to changes in assumptions is primarily due to a fall in corporate bond yields combined with an increase in the expected inflation rate which have combined to reduce the real discount rates used to calculate the liabilities of the pension plans as at 31 December 2009.

The curtailment gain recognised in the year relates to pension benefit restructuring in the US.

Contributions

The Group contributions made to the defined benefit plans in the year ended 31 December 2009 were £546m (2008 £399m) excluding those amounts allocated to equity accounted investments and participating employers (£91m). This includes an incremental contribution of $250m (£160m) which the Group made to the US pension schemes during the year. In 2010, the Group expects to make regular contributions at a similar level to those made in 2009.

The Group incurred a charge in respect of the cash contributions of £127m (2008 £84m) paid to defined contribution plans for employees. It expects to make a contribution of £141m to these plans in 2010.

During the year, the Group contributed £225m into Trust for the benefit of the Group's main pension scheme. The contribution is reported within other investments – current (£211m after a fair value gain of £2m) and cash and cash equivalents (£16m) in the consolidated balance sheet at 31 December 2009, and the use of these assets is restricted under the terms of the Trust. However, the Group considers this contribution to be equivalent to the other one-off contributions it makes into the Group's pension schemes and, accordingly, presents below a definition of the pension deficit to include this contribution.

	31 December 2009 £m
Group's share of IAS 19 deficit	**(4,637)**
Assets held in Trust	**227**
Pension deficit as defined by the Group	**(4,410)**

6. Dividends

Equity dividends	**2009 £m**	2008 £m
Prior year final 8.7p dividend per ordinary share paid in the year (2008 7.8p)	**307**	274
Interim 6.4p dividend per ordinary share paid in the year (2008 5.8p)	**227**	204
	534	478

After the balance sheet date, the directors proposed a final dividend of 9.6p (2008 8.7p). The dividend, which is subject to shareholder approval, will be paid on 1 June 2010 to shareholders registered on 23 April 2010. The ex-dividend date is 21 April 2010.

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 2010.

7. Acquisitions and disposals

Acquisition of subsidiaries for the year ended 31 December 2009

The most significant acquisition made by the Group during the year ended 31 December 2009 was of the 45% shareholding in BVT Surface Fleet Limited (BVT) held by VT Group plc (VT). If the acquisition had occurred on 1 January 2009, combined sales of Group and equity accounted investments would have been £22.8bn, revenue £21.3bn and loss for the year ended 31 December 2009 £58m.

BVT (now BAE Systems Surface Ships)

On 30 October 2009, the BVT joint venture became a wholly-owned subsidiary of the Group after VT Group plc exercised its option to sell its 45% shareholding in BVT to BAE Systems. Consideration paid including transaction costs for the remaining 45% interest was £348m. The now wholly-owned company has been renamed BAE Systems Surface Ships Limited (Surface Ships). The Group previously held a 55% interest in BVT, and accounted for its share of the results and net assets of BVT in accordance with IAS 31, *Interests in Joint Ventures*.

Total provisional goodwill arising amounted to £584m. This consists of £225m which arose on the initial formation of the BVT joint venture in the year ended 31 December 2008 and £359m arising on the acquisition of the 45% interest.

In the period from acquisition to 31 December 2009, Surface Ships contributed revenue and profit after tax of £338m and £34m, respectively, to the Group's consolidated results as a wholly-owned subsidiary.

Surface Ships is a leading designer, manufacturer and integrator of surface ships and their support vessels. It delivers complex engineering, integration and through-life support across the lifecycle of a ship. Bringing Surface Ships into full ownership of BAE Systems further strengthens the Group's global maritime business and is consistent with the strategy to establish a sustainable and profitable through-life business in air, land and sea. Surface Ships has a solid order book, a clear strategy to transform the UK maritime sector and a commitment to deliver existing and future programmes.

The acquisition of BVT had the following effect on the Group's assets and liabilities. The figures in the table below represent a 100% interest in BVT.

	Book value £m	Accounting policy alignments £m	Fair value adjustments £m	Fair value £m
Intangible assets	–	–	225	225
Property, plant and equipment	136	–	–	136
Inventories	61	–	–	61
Receivables	225	–	–	225
Deferred tax assets	2	–	3	5
Payables	(433)	–	(164)	(597)
Current tax liabilities	(16)	–	–	(16)
Deferred tax liabilities	(6)	–	(63)	(69)
Provisions	(12)	–	–	(12)
Cash and cash equivalents	33	–	–	33
Net (liabilities)/assets acquired	**(10)**	**–**	**1**	**(9)**
Goodwill				**584**
Fair value of net liabilities acquired and goodwill arising				**575**

Components of cost of acquisitions:	
Fair value of consideration for initial 55% shareholding in 2008	189
Fair value of consideration for remaining 45% shareholding in 2009	348
Total cost of acquisition	537
Losses under equity method of initial 55% shareholding	(36)
Gain on revaluation of step acquisition	74
Fair value of net liabilities acquired and goodwill arising	575

Consideration satisfied by:	
Cash paid on acquisition of remaining 45% shareholding in 2009	346
Directly attributable costs:	
Paid	2
Cash consideration	348
Fair value of net assets contributed to BVT joint venture for initial 55% shareholding in 2008	178
Directly attributable costs:	
Paid	11
Total cost of acquisition	537

The intangible assets acquired as part of the acquisition of BVT can be analysed as follows:

	£m
Order backlog	225
	225

NOTES TO THE ACCOUNTS *CONTINUED*

7. Acquisitions and disposals *continued*

Advanced Ceramics Research
The Group acquired Advanced Ceramics Research, Inc. in the US on 8 June 2009 for a consideration of $14m (£9m). The net assets and goodwill included in the Group's consolidated balance sheet as a result of this acquisition are £1m and £8m, respectively.

Acquisition of subsidiaries for the year ended 31 December 2008
During the year ended 31 December 2008, the Group acquired MTC Technologies, Inc., Tenix Defence Holdings Pty Limited, Tenix Toll Defence Logistics Pty Limited, Detica Group plc and IST Dynamics. Certain of the fair values assigned to the net assets at the dates of acquisition were provisional, and in accordance with IFRS 3, *Business Combinations*, the Group has adjusted the fair values attributable to these acquisitions in the year ended 31 December 2009, resulting in a net increase in goodwill of £5m. This has not had a material impact on the consolidated accounts and, as such, the Group has not restated the balance sheet as at 31 December 2008.

Disposals
Continuing operations for the year ended 31 December 2009
Profit on disposal of businesses of £68m comprises the finalisation of the accounting gain recognised in 2008 on the disposal of the Group's interests in the businesses contributed to the BVT joint venture following acquisition of VT Group's 45% interest in 2009 (£58m) and additional proceeds received in respect of the disposal in 2008 of the Group's interest in Flagship Training (£10m).

The Group received deferred consideration of £72m in the year ended 31 December 2009 in respect of the disposals of Flagship Training Limited in 2008 (£70m) and the Inertial Products business in 2007 (£2m).

Continuing and discontinued operations for the year ended 31 December 2008

Name	Country of incorporation	Date of sale	Percentage share	Profit on disposal of businesses £m	Proceeds from sale of subsidiary undertakings £m	Proceeds from sale of equity accounted investments £m	Deferred consideration £m
Surveillance & Attack division	USA	22.02.08	100%	61	118	–	–
BAE Systems Surface Fleet Solutions Limited[1]	UK	01.07.08	45%	121	–	–	–
Flagship Training Limited[2]	UK	01.07.08	50%	56	–	16	53
Gregory backpack business	USA	14.03.08	100%	–	7	–	–
Continuing operations				238	125	16	53
Discontinued operations[3] – Mobile International business	USA	14.02.08	100%	–	6	–	–
				238	131	16	53

1 On 1 July 2008, the Group exchanged a 45% shareholding in BAE Systems Surface Fleet Solutions Limited (SFSL) as consideration for the contribution to SFSL of 100% of VT Group plc's shipbuilding and naval support businesses to form the joint venture BVT Surface Fleet Limited.
2 Discounted consideration of £67m had been deferred over three years, the discounted value of which was £53m and is included within other receivables at 31 December 2008.
3 The Group's Mobile International business was acquired with Armor Holdings, Inc. on 31 July 2007 with a view to immediate resale. Accordingly, it was classified as held for sale as at 31 December 2007. The sale was completed on 14 February 2008 for a cash consideration less transaction costs of £6m.

Cash flows in relation to acquisitions and disposals

	Subsidiaries					Equity accounted investments		
	BVT £m	Advanced Ceramics Research £m	**Total acquisitions £m**	Inertial Products £m	**Total disposals £m**	Flagship Training £m	Diamond Detectors £m	**Total £m**
Cash (consideration)/proceeds	(348)	(9)	**(357)**	2	**2**	70	(1)	**(286)**
Cash and cash equivalents net of overdrafts acquired	33	–	**33**	–	**–**	–	–	**33**
Acquisitions and disposals	(315)	(9)	**(324)**	2	**2**	70	(1)	**(253)**
Debt acquired on acquisition of subsidiary	–	(1)	**(1)**	–	**–**	–	–	**(1)**
	(315)	(10)	**(325)**	2	**2**	70	(1)	**(254)**

8. Related party transactions

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

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

	31 December 2009 £m	31 December 2008 £m
Sales to related parties	**1,241**	1,081
Purchases from related parties	**426**	147
Amounts owed by related parties	**207**	200
Amounts owed to related parties	**1,353**	1,476

9. Events after the balance sheet date

On 5 February 2010, the Group announced a global settlement with the US Department of Justice and the UK's Serious Fraud Office in respect of investigations announced by these two authorities in 2007 and 2004, respectively. This is an adjusting event after the balance sheet date in accordance with IAS 10, *Events after the Reporting Period*, and, accordingly, the penalties totalling £278m have been reflected in the Group's accounts for the year ended 31 December 2009.

On 15 February 2010, the Group announced that it had been informed that the decision by the US Department of Defense not to award a follow-on contract for production of vehicles under the Family of Medium Tactical Vehicles (FMTV) programme to BAE Systems had been confirmed. This is an adjusting event after the balance sheet date in accordance with IAS 10 and, accordingly, impairment of goodwill and other intangible assets amounting to £592m relating to the Armor Holdings, Inc. transaction and specifically the FMTV product line have been reflected in the Group's accounts for the year ended 31 December 2009.

10. Annual General Meeting

This year's Annual General Meeting will be held on 5 May 2010. 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 2010.

11. Other information

The financial information for the years ended 31 December 2009 and 31 December 2008 contained in this preliminary announcement was approved by the Board on 17 February 2010. This announcement does not constitute statutory accounts of the Company within the meaning of section 435 of the Companies Act 2006.

Statutory accounts for the year ended 31 December 2008 have been delivered to the Registrar of Companies. Statutory accounts for the year ended 31 December 2009 will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

The auditors have reported on both these sets of accounts. Their reports were not qualified and did not contain a statement under section 237(2) or (3) of the Companies Act 1985 in respect of the year ended 31 December 2008 and section 498(2) or (3) of the Companies Act 2006 in respect of the year ended 31 December 2009.

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