HALF-YEARLY REPORT 2013

BAE SYSTEMS

Cautionary statement:
All statements other than statements of historical fact included in this document, including, without limitation, those regarding the financial condition, results, operations and businesses of BAE Systems and its strategy, plans and objectives and the markets and economies in which it operates, are forward-looking statements. Such forward-looking statements which reflect management's assumptions made on the basis of information available to it at this time, involve known and unknown risks, uncertainties and other important factors which could cause the actual results, performance or achievements of BAE Systems or the markets and economies in which BAE Systems operates to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. BAE Systems plc and its directors accept no liability to third parties in respect of this report save as would arise under English law. Accordingly, any liability to a person who has demonstrated reliance on any untrue or misleading statement or omission shall be determined in accordance with section 90A of the Financial Services and Markets Act 2000. It should be noted that section 90A contains limits on the liability of the directors of BAE Systems plc so that their liability is solely to BAE Systems plc.

RESULTS IN BRIEF, FINANCIAL KEY POINTS AND OUTLOOK

Results in brief

	Six months ended 30 June 2013	Restated[1] Six months ended 30 June 2012	Restated[1] Year ended 31 December 2012
Results from continuing operations			
Sales[2]	**£8,448m**	£8,334m	£17,834m
Underlying EBITA[3]	**£865m**	£922m	£1,856m
Operating profit	**£750m**	£768m	£1,599m
Underlying earnings[4] per share	**17.8p**	18.6p	38.5p
Basic earnings per share[5]	**12.6p**	12.8p	29.1p
Order backlog[2,6]	**£43.1bn**	£40.0bn	£42.4bn
Other results including discontinued operations			
Dividend per share	**8.0p**	7.8p	19.5p
Operating business cash flow[7]	**£(815)m**	£742m	£2,692m
Net (debt)/cash (as defined by the Group)[8]	**£(1,192)m**	£(1,230)m	£387m

Financial key points

- Sales[2] increased by 1%
- Underlying EBITA[3] decreased by 6%. Deferred recognition of sales and profit relating to the formalisation of price escalation on the Salam Typhoon programme
- Underlying earnings[4] per share decreased by 4%
- Order backlog[2,6] increased to £43.1bn
- Non-UK and US order intake[2] of £4.8bn in the period
- Interim dividend increased by 3% to 8.0p per share
- Operating business cash outflow[7] of £815m

Outlook

Group

In aggregate, including both the benefit from the share repurchase programme and downside arising from reductions to US defence budgets, double-digit growth in underlying earnings[4] per share is anticipated for 2013. This outlook assumes the satisfactory conclusion to Salam pricing negotiations this year.

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

Reporting segments

- Electronic Systems sales[2,9] are expected to be marginally below those for 2012 with margins expected to be lower within a range of 12% to 14%.
- Cyber & Intelligence sales[2,9] are expected to be some 5% lower than those in 2012 with margins expected to be within an 8% to 9% range.
- In Platforms & Services (US), Land & Armaments sales[2,9] are expected to decrease towards a $3.6bn level with margins around 8%. Support Solutions sales[2,9] are expected to be around those for 2012, with margins expected to be similar to those delivered in the first half of 2013.
- Platforms & Services (UK) sales[2] in 2013 are expected to increase by around 25%, assuming a price escalation settlement on the Salam Typhoon contract. Margins are expected to be slightly higher than those in 2012.
- Platforms & Services (International) sales[2] are expected to be marginally higher than in 2012. Margins are expected to benefit from the anticipated resolution of Salam Typhoon price escalation, and are expected to be towards the higher end of a 10% to 12% range.

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.
2 Including share of equity accounted investments.
3 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 3).
4 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).
5 Basic earnings per share in accordance with International Accounting Standard 33, Earnings per Share.
6 Order backlog comprises funded and unfunded unexecuted customer orders, and is stated after the elimination of intra-group orders.
7 Net cash (outflow)/inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.
8 See definition on page 4.
9 In US dollars.

INTERIM MANAGEMENT REPORT

The Group’s sales in the first half of 2013 include resumption of Typhoon aircraft deliveries to Saudi Arabia under the Salam programme offset by the anticipated reduction in land activity. First half margins reflect deferred profit trading on those Salam Typhoon deliveries. The first half of 2012 included the benefit of strong programme execution and risk reduction on the European Typhoon production and Type 45 destroyer programmes.

The Group’s first half results reflect significant anticipated trading bias towards the second half of the year. Assuming a satisfactory conclusion to Salam Typhoon pricing negotiations this year, the second half performance will include the deferred trading from prior aircraft deliveries together with the cumulative benefit of the continuing deliveries.

With constraints in many of the Group’s principal markets, cost reduction continues to be a focus for BAE Systems, to protect margin, enhance competitive advantage and deliver greater affordability for customers. Despite these pressures, focused investment in research and technology, and business development continue as a priority.

UK
Notwithstanding the continued pressure on many areas of government spend in the UK, the outlook for the Group’s UK defence business remains stable. Much of the Group’s UK business is concentrated on a small number of large programmes where multi-year contracts provide good visibility, as evidenced by the large UK order backlog. Discussions continue with the Ministry of Defence to balance naval surface shipbuilding capacity with future warship demand.

US
Performance of the Group’s US-based businesses was impacted by pressure on US government spending and the introduction of budget Sequestration measures resulting in continued significant defence budget uncertainty.

In March, legislation was passed to set defence funding levels for the remainder of the 2013 Fiscal Year, which allowed some limited flexibility to enable near-term priorities to be pursued.

In April, the Presidential Request for a Fiscal Year 2014 budget, which would replace Sequestration with a range of spending cuts and tax increases, was tabled by the US Congress. At this time, there is no consensus to pass this type of comprehensive budget resolution.

Unless measures are introduced to mitigate the impact of Sequestration, defence spend is expected to face continued reduction.

International
International market activity remains strong with significant opportunities being pursued. Building on the international order intake in 2012, a further £4.8bn of non-UK/US orders were received in the first half of the year.

A key feature of the anticipated trading profile across the year is formalising the contractual price escalation obligations under the Salam Typhoon contract in the Kingdom of Saudi Arabia, relating to agreements signed in 2007. Four Typhoon aircraft were delivered in the first half, adding to the initial phase of 24 Typhoon aircraft deliveries between 2009 and the end of 2011. The Group’s objective remains that of concluding appropriate terms.

Notwithstanding the price escalation discussions, the Group continues to develop its business in Saudi Arabia. Order intake in the first half included a £0.6bn weapons contract, awarded in March under the Saudi British Defence Co-operation Programme, and an order in June, valued at approximately £1.8bn, for follow-on support through to 2017 on the Salam Typhoon programme.

M&A activity
In February, the Group completed the sale of its Commercial Armored Vehicles LLC business in West Chester, Ohio, to The O’Gara Group, Inc. for cash consideration of approximately $10m (£6m).

The conditions to closing the November 2012 agreement to acquire Marine Hydraulics International, Inc., a US marine repair, overhaul and conversion company, have not been satisfied and the agreement has now been terminated.

Balance sheet and capital allocation
The Group's balance sheet continues to be managed conservatively in line with the Group's policy to retain its investment grade credit rating and to ensure operating flexibility.

Consistent with this approach, the Group expects to continue to meet its pension obligations, pursue organic investment opportunities, plans to pay dividends in line with its policy of long-term sustainable cover of around two times underlying earnings and to make accelerated returns of capital to shareholders when the balance sheet allows. Investment in value-enhancing acquisitions will be considered where market conditions are right and where they deliver on the Group's strategy.

With the announcement of the full year results in February, the Group initiated a share repurchase programme of up to £1bn over three years. Full implementation of the programme remains subject to satisfactory resolution of the Salam Typhoon price escalation negotiations. As at 30 June, BAE Systems had purchased 24 million shares for approximately £90m under the programme.

Accounting change
With effect from 1 January 2013, the Group has adopted International Accounting Standard 19 (revised 2011), Employee Benefits. This replaces interest cost and expected return on plan assets with a finance cost on the pension deficit calculated using the rate currently used to discount defined benefit pension liabilities and requires certain administration costs to be included within underlying EBITA. Comparative financial information in this report has been restated accordingly and more information on the accounting change is provided in note 1 to the Group accounts on page 18.

Directors and management
In May, Sir Peter Mason, a non-executive director, retired from the Board of BAE Systems plc and Ian Tyler joined the Board as a non-executive director of the Company.

The Chairman, Dick Olver, was awarded a knighthood in the Queen’s Birthday Honours in June for his contributions both to British industry and to the development of corporate governance in the UK.

In June, the Group announced that Sir Roger Carr would join the Board of BAE Systems plc as a non-executive director and Chairman designate on 1 October 2013 and would succeed Sir Richard Olver as Chairman in the first quarter of 2014. Also in June, Chris Grigg was appointed a non-executive director of the Company with effect from 1 July.

At the end of March, Larry Prior, Executive Vice President, Service Sectors, for BAE Systems, Inc. and a member of the Executive Committee, left the Group to pursue other opportunities. He has been replaced in those roles by David Herr, formerly President, BAE Systems Support Solutions.

Dividend
The Board has declared a 3% increase in the interim dividend to 8.0p for the first half year to 30 June 2013. At this level, the dividend is covered 2.2 times by underlying earnings, consistent with the Group's policy of long-term sustainable cover of around two times.

Summarised income statement – continuing operations

	Six months ended 30 June 2013 £m	Restated[1] Six months ended 30 June 2012 £m
Sales[2]	**8,448**	8,334
Underlying EBITA[3]	**865**	922
Profit on disposal of businesses	**4**	18
EBITA	**869**	940
Amortisation of intangible assets	**(96)**	(101)
Impairment of intangible assets	**(4)**	(63)
Finance costs[2]	**(223)**	(192)
Taxation expense[2]	**(133)**	(161)
Profit for the period	**413**	423
Underlying earnings[4] per share	**17.8p**	18.6p
Basic earnings per share[5]	**12.6p**	12.8p
Dividend per share	**8.0p**	7.8p

Exchange rates – average

£/$	**1.544**	1.577
£/€	**1.175**	1.216
£/A$	**1.524**	1.528

Exchange rates – period end

£/$	**1.517**	1.569
£/€	**1.167**	1.237
£/A$	**1.657**	1.531

Exchange rates – year end	31 December 2012
£/$	1.624
£/€	1.232
£/A$	1.564

Segmental analysis – continuing operations

	Sales[2]		Underlying EBITA[3]	
	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m	Six months ended 30 June 2013 £m	Restated[1] Six months ended 30 June 2012 £m
Electronic Systems	**1,194**	1,181	**156**	164
Cyber & Intelligence	**657**	714	**53**	54
Platforms & Services (US)	**2,085**	2,254	**182**	189
Platforms & Services (UK)	**3,192**	2,651	**384**	420
Platforms & Services (International)	**1,654**	1,573	**165**	161
HQ*	**145**	123	**(75)**	(66)
Intra-group	**(479)**	(162)	**–**	–
	8,448	8,334	**865**	922

* In 2013, the HQ reporting segment includes a £32m charge in respect of a contract pricing dispute.

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

Income statement – continuing operations

Sales[2] in the first half of 2013 were £8,448m (2012 £8,334m), 1% higher than 2012 on a like-for-like basis, after adjusting for the impact of exchange translation and M&A. This mainly reflects the benefit of the resumption of aircraft deliveries on the Salam Typhoon programme offset by the anticipated reduction in land activity. Sales[2] in 2013 are expected to have a second half bias.

Underlying EBITA[3] was £865m (2012 £922m) giving a return on sales of 10.2% (2012 11.1%).

Non-recurring items are defined as items relevant to an understanding of the Group's performance with reference to their materiality and nature. The non-recurring items are excluded from underlying EBITA[3]. **Profit on disposal of businesses** of £4m (2012 £18m) includes the disposal of the Commercial Armored Vehicles business, which was part of Land & Armaments.

Amortisation of intangible assets was £96m (2012 £101m).

Impairment of intangible assets of £63m in 2012 related to the Safariland and Tensylon businesses sold in July 2012.

Finance costs[2] were £223m (2012 £192m). The underlying interest charge, excluding pension accounting, marked-to-market revaluation of financial instruments and foreign currency movements, was £95m (2012 £91m).

Taxation expense[2] reflects the Group's effective tax rate for the period of 25% (2012 27%). The effective tax rate is based on profit before taxation excluding profit on disposal of businesses. The effective tax rate for the full year is expected to be in the range of 23% to 25%, with the final number dependent on the geographical mix of profits.

Underlying earnings[4] per share for the period decreased by 4% to 17.8p compared with 2012 (18.6p).

Basic earnings per share[5] for the period was 12.6p (2012 12.8p).

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.
2 Including share of equity accounted investments.
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4 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).
5 Basic earnings per share in accordance with International Accounting Standard 33, Earnings per Share.

INTERIM MANAGEMENT REPORT CONTINUED

Reconciliation of cash flow from operating activities[6] to net debt (as defined by the Group)

	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m
Cash (outflow)/inflow from operating activities[6]	**(728)**	940
Capital expenditure (net) and financial investment	**(97)**	(189)
Dividends received from equity accounted investments	**10**	16
Assets contributed to Trust	**–**	(25)
Operating business cash flow	**(815)**	742
Interest	**(81)**	(68)
Taxation	**(94)**	(56)
Free cash flow	**(990)**	618
Acquisitions and disposals	**6**	18
Net purchase of own shares	**(90)**	(16)
Equity dividends paid	**(380)**	(367)
Dividends paid to non-controlling interests	**(12)**	(11)
Cash flow from matured derivative financial instruments	**33**	(49)
Movement in cash collateral	**2**	–
Foreign exchange translation	**(170)**	16
Other non-cash movements	**22**	–
Total cash (outflow)/inflow	**(1,579)**	209
Opening net cash/(debt) (as defined by the Group)	**387**	(1,439)
Closing net debt (as defined by the Group)	**(1,192)**	(1,230)
Comprising:		
Debt-related derivative financial assets	**38**	56
Cash and cash equivalents	**1,919**	2,464
Loans – non-current	**(2,809)**	(3,054)
Loans and overdrafts – current	**(338)**	(265)
Less: Cash received on customers' account[7]	**(2)**	(3)
Less: Assets held in Trust	**–**	(428)
Net debt (as defined by the Group)	**(1,192)**	(1,230)

Operating business cash flow

	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m
Electronic Systems	**73**	105
Cyber & Intelligence	**56**	21
Platforms & Services (US)	**(89)**	–
Platforms & Services (UK)	**(415)**	243
Platforms & Services (International)	**(221)**	568
HQ	**(223)**	(188)
Discontinued operations	**4**	(7)
Operating business cash flow	**(815)**	742

Cash flows

Cash outflow from operating activities[6] was £728m (2012 inflow £940m), which includes contributions in excess of service costs for the UK and US pension schemes totalling £192m (2012 £211m).

As anticipated, advances are being consumed on the Omani Typhoon and Hawk programme, the European Typhoon contract and the Saudi training aircraft contract. 2012's accelerated receipts on the Saudi Tornado upgrade programme are also being utilised. Costs incurred on the Oman Offshore Patrol Vessel contract and on rationalisation are being charged against the provisions created in previous years. The £131m Trinidad and Tobago termination settlement was paid in the period.

Dividends received from equity accounted investments, comprising Eurofighter and FADEC International, amounted to £10m (2012 £16m).

Taxation payments were £38m higher at £94m primarily reflecting tax refunds in 2012 following the 2011 Research & Development tax settlement and timing differences on US tax payments.

Net cash inflow in respect of **acquisitions and disposals** of £6m mainly comprises the disposal of Commercial Armored Vehicles. The net cash inflow in 2012 mainly comprised the disposal of the Safety Products business.

The **net purchase of own shares** of £90m (2012 £16m) includes shares purchased and cancelled under the share repurchase programme announced in February.

Foreign exchange translation during the period, primarily in respect of the Group's US dollar-denominated borrowing, increased reported net debt by £170m.

Net debt (as defined by the Group)

The Group's net debt at 30 June 2013 was £1,192m (30 June 2012 £1,230m), a net outflow of £1,579m from the net cash position of £387m at the start of the period. Cash and cash equivalents of £1.9bn (30 June 2012 £2.5bn) are held primarily for the share repurchase programme, pension deficit funding, payment of the 2013 interim dividend, repayment of £0.4bn of debt securities maturing in 2014 and management of working capital.

Going concern

After making due enquiries, the directors have a reasonable expectation that the Group has adequate resources to continue operational existence for the foreseeable future and therefore continue to adopt the going concern basis in preparing the accounts.

Principal risks

The principal risks facing the Group for the remaining six months of the year are unchanged from those reported in the Annual Report 2012.

These risks, together with the Group's risk management process, are detailed on pages 44 to 51 of the Annual Report 2012, and relate to the following areas: defence spending; government customers; global market; contract award timing; large contracts; fixed-price contracts; component availability, subcontractor performance and key suppliers; laws and regulations; competition; pension funding; export controls and other restrictions; acquisitions; consortia and joint ventures; exchange rates; and cybersecurity.

6 2012 excludes the £29.5m charitable contribution made in 2012 for the benefit of the people of Tanzania in connection with the global settlement with the UK's Serious Fraud Office in 2010 as the amount had been deducted from the Group's net debt in 2010.
7 Cash received on customers' account is the unexpended cash received from customers in advance of delivery which is subject to advance payment guarantees unrelated to Group performance. It is included within trade and other payables in the consolidated balance sheet.

REPORTING SEGMENTS: ELECTRONIC SYSTEMS

Electronic Systems, with 12,600 employees[1], comprises the US and UK-based electronics activities, including electronic warfare systems and electro-optical sensors, military and commercial digital engine and flight controls, next-generation military communications systems and data links, persistent surveillance capabilities, and hybrid electric drive systems.

	Six months ended 30 June 2013	Six months ended 30 June 2012	Year ended 31 December 2012
Sales[1]	**£1,194m**	£1,181m	£2,507m
Underlying EBITA[2]	**£156m**	£164m	£356m
Return on sales	**13.1%**	13.9%	14.2%
Cash inflow[3]	**£73m**	£105m	£256m
Funded order intake[1]	**£1,124m**	£1,133m	£2,540m
Order backlog[1,4]	**£3.7bn**	£3.6bn	£3.6bn

Financial performance

Despite the ongoing US budget uncertainties and some related programme delays and disruptions, Electronic Systems delivered sales[1] of $1.8bn (£1.2bn), only 1% down compared to the first half of 2012.

Sales[1] in the commercial areas of the business grew by 10%, helping to offset some of the pressures on the defence side.

The return on sales achieved of 13.1% was in the middle of the guidance range.

Cash conversion of underlying EBITA[2] in the first half year was at 47% and the business expects an improved conversion level over the full year.

The order backlog[1,4] of $5.7bn (£3.7bn) was marginally down from the start of the year.

Operational performance

Electronic Combat
Electronic Systems maintains its leadership position in the US electronic warfare market. The flight test programme for the electronic warfare suite on the F-35 Lightning II programme commenced during the period. The business completed Low-Rate Initial Production (LRIP) Lot 5 deliveries and continued Lot 6 deliveries. BAE Systems has been awarded a $140m (£92m) contract for LRIP Lot 7, which includes production aircraft for international customers.

The business completed its technology maturation contract on the US Navy's Next-Generation Jammer programme. BAE Systems was not awarded a contract for the technology development phase of the programme.

Under contracts totalling over $0.9bn (£0.6bn), the Digital Electronic Warfare System (DEWS) will be installed on 84 new F-15 aircraft with upgrades to 70 existing F-15 aircraft for the Royal Saudi Air Force. Initial flight testing is scheduled to begin in November. BAE Systems continues to pursue other export opportunities for the DEWS suite.

Survivability & Targeting
The business continues to execute its $38m (£25m) Common Infrared Countermeasures technical development contract. Testing of initial units is in progress, with the first deliveries planned ahead of schedule.

The Advanced Precision Kill Weapon System demonstrated its versatility, with successful testing on several new platforms for the US Air Force, Navy and Marines. The business continues to execute its $69m (£45m) Full-Rate Production contract.

The Terminal High-Altitude Area Defence system successfully engaged a medium-range target during a complex missile defence test.

BAE Systems was awarded a $15m (£10m) contract to support the US Army's Joint Effects Targeting System programme. The contract initiates a three-year engineering and manufacturing development phase, which will be followed by an LRIP award competition.

Communications & Control
The PHOENIX™-SC radio was proposed for the US Army's next-generation Mid-tier Networking Vehicular Radio competition, which has a projected total lifecycle value greater than $2bn (£1.3bn). The award decision is expected in the second half of the year.

The business continues to develop its family of display products, receiving contracts for LRIP Lots 6 and 7 on the F-35 Lightning II Active Inceptor System.

Intelligence, Surveillance & Reconnaissance (ISR)
Electronic Systems continues to provide Wide Area Airborne Surveillance capability for the US Air Force and US Army based on two wide-area, high-resolution imaging sensor systems, the Autonomous Real-time Ground Ubiquitous Surveillance – Imaging System and the Airborne Wide Area Persistent Surveillance System.

1 Including share of equity accounted investments.
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3 Net cash inflow from operating activities after capital expenditure (net) and financial investment, dividends from equity accounted investments, and assets contributed to Trust.
4 Order backlog comprises funded and unfunded unexecuted customer orders.

INTERIM MANAGEMENT REPORT CONTINUED
REPORTING SEGMENTS: ELECTRONIC SYSTEMS CONTINUED

The business is providing state-of-the-art processing capabilities for the US Navy's P-8A Poseidon programme and progressing the first lot of Full-Rate Production. The mission computer suite provides high performance in the military environment.

In the Identification Friend or Foe market, BAE Systems has been awarded a $34m (£22m) contract to provide its enhanced Combined Interrogator Transponder system to the US Air Force and participating European air force partners.

Commercial Aircraft electronics
BAE Systems and its partner, Sagem, marked a ten-year milestone for their joint venture, FADEC International, which has fielded nearly 10,000 Full-Authority Digital Engine Controls (FADEC) recording over 625 million hours aboard global airliners. It is developing the next-generation FADEC for CFM International's LEAP and GE Aviation's Passport engines, with the first flight-worthy units delivered for the Passport's first-engine-to-test during the period.

The business has been selected by Boeing to provide several subsystems, including the spoiler control electronics, for the new Boeing 737 MAX, with a total potential value of $1bn (£0.7bn) over the life of the aircraft programme.

The business continues to pursue opportunities in China and other emerging markets for its avionics products and services for the civil market.

HybriDrive® propulsion
Orders for more than 500 HybriDrive® diesel-electric propulsion systems were received during the period, worth in excess of $70m (£46m). In the US, the Santa Clara Valley Transit Agency awarded New Flyer Industries an order for 29 hybrid articulated transit buses featuring the new HDS300 HybriDrive® Series Propulsion System. BAE Systems will provide propulsion systems for 475 Nova buses for Quebec.

Looking forward

Efforts to reduce the US government's budget deficit are likely to impact all areas of government spend. Whilst legislation was passed in March to set defence funding levels for the remainder of the 2013 Fiscal Year, a Continuing Resolution for the 2014 Fiscal Year is likely and the impact of Sequestration remains uncertain.

Whilst likely funding reductions and the resultant slow down or cancellation of ongoing and new programmes could impact the business, Electronic Systems continues to be well-positioned to react to changing US Department of Defense priorities with its balanced portfolio of programmes and customers, and its sustained emphasis on cost reduction.

The business expects to benefit from its incumbent positions and ability to provide capability upgrades on platforms, and from positions in areas such as commercial aircraft electronics and international defence programmes.

REPORTING SEGMENTS: CYBER & INTELLIGENCE

Cyber & Intelligence, with 8,000 employees[1], comprises the US-based Intelligence & Security business and UK-headquartered BAE Systems Detica business, and covers the Group's cyber, secure government, and commercial and financial security activities.

	Six months ended 30 June 2013	Six months ended 30 June 2012	Year ended 31 December 2012
Sales[1]	**£657m**	£714m	£1,402m
Underlying EBITA[2]	**£53m**	£54m	£124m
Return on sales	**8.1%**	7.6%	8.8%
Cash inflow[3]	**£56m**	£21m	£113m
Funded order intake[1]	**£610m**	£736m	£1,454m
Order backlog[1,4]	**£0.9bn**	£1.0bn	£1.0bn

Financial performance

In aggregate, sales[1] reduced by some 10% to just over $1bn (£657m). The US business saw a 14% decrease driven largely by reduced volumes in the IT Solutions business and lower levels of analysis support on Counter-Improvised Explosive Device activity in Afghanistan. Growth in the BAE Systems Detica business was 9%.

The margin achieved at the half year of 8.1% includes continued organic investment in the BAE Systems Detica business in support of targeted future growth in commercial and international markets.

Cash flow[3] performance was good with conversion in excess of underlying EBITA[2] in the first half.

Order backlog[1,4] reduced to $1.4bn (£0.9bn). US budget uncertainties continue to cause delay in award decisions of competitive bids. At the end of the period, there were some $2.1bn (£1.4bn) of tabled bids of which almost half were overdue against decision timescales.

Operational performance

Intelligence & Security

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

Work continues on the final option year of the Counter-Improvised Explosive Device programme, with a total value of funded orders of approximately $450m (£297m). The business has started to execute the follow-on Combat Intelligence Analytical Teams contract, with orders totalling approximately $150m (£99m) expected over the next three years, and continues to work with the customer to manage staffing levels in line with reducing mission requirements.

The business has won all task orders competed in the market for Full Motion Video Analysis during the period and continues to execute awarded contracts, which are worth over $400m (£264m) and include over 300 analysts supporting mission critical activities.

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

On the Solutions for the Information Technology Enterprise Indefinite Delivery, Indefinite Quantity contract, with task orders worth $344m (£227m), the business enables the US Defense Intelligence Agency to provide reliable, cost-effective and highly secure IT services to over 50,000 Department of Defense personnel worldwide.

Work continued on the $60m (£40m) Next-Generation Desktop Environment programme for the US Defense Intelligence Agency providing an enterprise networking environment based on virtual desktop infrastructure to change the way applications are delivered to user desktops.

In January, the business was awarded a $127m (£84m) contract to support the US National Security Agency's High Performance Computing Infrastructure Group with architecture, installation and administration for a complex networking environment supporting multiple network enclaves and high-speed data centre access. Under the contract, both server and desktop computer support will be provided to more than 3,000 end users.

Geospatial Intelligence – Intelligence, Surveillance and Reconnaissance (GEOINT-ISR) develops software platforms and mission systems for the US defence and intelligence communities.

The business provides activity-based intelligence systems that support missions for the National Geospatial-Intelligence Agency under an initial $60m (£40m) award in 2012, and is promoting these solutions to other US intelligence and defence agencies.

In April, the business was awarded a $62m (£41m) contract for the Mobility Air Force Automated Flight Planning Service programme to develop and sustain a new air vehicle flight planning and route optimisation capability for the US Air Force's Tanker Airlift Control Center.

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 3).
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 Order backlog comprises funded and unfunded unexecuted customer orders.

INTERIM MANAGEMENT REPORT CONTINUED
REPORTING SEGMENTS: CYBER & INTELLIGENCE CONTINUED

BAE Systems Detica

BAE Systems Detica delivers information intelligence solutions to protect and enhance customers' operations in the areas of cyber security, financial crime and communications intelligence.

Cyber Security

The Detica CyberReveal™ advanced cyber threat monitoring product was launched in April and has been deployed by a major global financial institution. Managed security services delivered from the Security Operations Centre in the UK continue to gain traction, with BAE Systems Detica named as official cyber security partner to McLaren in April.

Detica MobileProtect™, a cloud-based service for securing smart devices, has been launched alongside a five-year strategic partnership with Vodafone, initially to provide Vodafone's largest enterprise customers with the Vodafone Mobile Threat Manager solution. Vodafone is in the process of launching the product globally, with a number of customer trials underway.

NetReveal

BAE Systems Detica continues to provide enterprise risk, fraud and compliance solutions internationally, with new business wins from customers, including Commerzbank, Home Trust Company and Zurich, contributing towards total order intake of £42m in the period. The Detica NetReveal™ solution continues to win industry recognition in the sector.

Communications Solutions

The business is a provider of end-to-end communications intelligence solutions to government and telecommunications operators internationally and is addressing opportunities in the Middle East and Asia Pacific regions.

UK Services

The consulting, systems integration and managed services business has been selected as preferred bidder by the Foreign & Commonwealth Office for its Service Management Integration framework, worth up to £80m over six years, and has signed a four-year IT Solutions and Systems Integration framework with Network Rail.

Looking forward

Efforts to reduce the US government's budget deficit are likely to impact all areas of government spend. Whilst legislation was passed in March to set defence funding levels for the remainder of the 2013 Fiscal Year, a Continuing Resolution for the 2014 Fiscal Year is likely and the impact of Sequestration remains uncertain.

Intelligence & Security has worked to reduce costs to balance government cuts, whilst pursuing growth opportunities, particularly in critical, mission-focused areas such as next-generation Intelligence, Surveillance and Reconnaissance, multiple intelligence fusion (the seamless synthesis of the individual intelligence disciplines to enable more complete situational awareness), counter intelligence and enterprise solutions for big data problems.

BAE Systems Detica expects continued growth from delivering information intelligence solutions in the UK and internationally, with demand from government and commercial customers for products and services which protect and enhance operations in the areas of cyber security, financial crime and communications intelligence.

REPORTING SEGMENTS: PLATFORMS & SERVICES (US)

Platforms & Services (US), with 20,900 employees[1], comprises the US-headquartered Land & Armaments business, with operations in the US, UK, Sweden and South Africa, together with the US-based Support Solutions business, which includes ship repair and munitions services.

	Six months ended 30 June 2013	Six months ended 30 June 2012	Year ended 31 December 2012
Sales[1]	**£2,085m**	£2,254m	£4,539m
Underlying EBITA[2]	**£182m**	£189m	£394m
Return on sales	**8.7%**	8.4%	8.7%
Cash (outflow)/inflow[3]	**£(89)m**	–	£314m
Funded order intake[1]	**£1,424m**	£2,616m	£5,010m
Order backlog[1,4]	**£7.8bn**	£9.1bn	£8.4bn

Financial performance

Support Solutions

Despite the budget uncertainties seen earlier in the year in the naval ship repair activity, sales[1] were 3% higher. The business benefited from the new business awards secured last year on the Radford Army Ammunition Plant and naval training aircraft maintenance.

Return on sales in the period at 8.0% was very similar to last year's level.

Cash flow[3] performance in the first half was impacted by timing of receipts in both the ship repair business and the Radford Army Ammunition Plant. A much stronger cash conversion of underlying EBITA[2] is therefore expected over the full year.

Order backlog[1,4] reduced from $5.4bn (£3.3bn) to $4.9bn (£3.2bn) on the trading out of long-term ship repair contracts.

Land & Armaments

Whilst reported sales[1] declined by 19%, that reduction on a like-for-like basis was 9%. This takes into account exchange translation, the impact of last year's business disposals and the transfer of the Combat Vehicles (UK) business to Platforms & Services (UK). As expected, the sales[1] reduction was largely from completion of contracts for Mine Resistant Ambush Protected vehicle upgrades.

The reported margin of 9.5% benefits from ongoing cost reduction actions and good programme execution. Charges for further planned rationalisation activity are expected in the second half year.

With regards to cash flow[3], performance will be second half biased due to the usual timing of funding on the UK munitions contract. In addition, funding on the Ground Combat Vehicle programme is back end loaded.

Order backlog[1,4] reduced from $8.3bn (£5.1bn) to $6.9bn (£4.6bn). $0.3bn (£0.2bn) of that reduction is due to exchange translation. Order award for India M777 is planned in the second half.

Operational performance

Support Solutions

During unexpected severe weather on 4 April, an employee fatality occurred at the Mobile, Alabama, shipyard when the Carnival Triumph cruise ship came free from its moorings. BAE Systems continues to co-operate with ongoing government investigations.

The conditional Worker Adjustment and Retraining Notification (WARN) Act notices issued in February to nearly 3,600 ship repair employees were largely mitigated by the funding legislation passed in March.

The US ship repair business was selected for a $49m (£32m) contract for the repair, maintenance and modernisation of the USS Porter, a US Navy destroyer.

In US commercial shipbuilding, Jackson Offshore Operators, LLC exercised an option under a contract signed in December 2012 for two additional platform supply vessels.

The business continues to provide infrastructure operations and management services at the Holston Army Ammunition Plant in the US and, in March, the US Army awarded an Indefinite Delivery, Indefinite Quantity contract valued at up to $780m (£514m) over five years to purchase explosives from the plant.

In 2012, the Republic of Korea selected BAE Systems to upgrade avionics and electronic systems on its fleet of more than 130 F-16 aircraft. The business is working to determine a scope of work that will satisfy the programme requirements, schedule and cost.

Support Solutions completed the transition to providing depot level maintenance and logistics support for US Navy T-34/T-44/T-6 training aircraft under a five-year contract awarded in November 2012. If all options are exercised, the contract would be valued at more than $400m (£264m) over five years.

BAE Systems is pursuing a bid for the US Air Force's T-X programme to replace the T-38 jet training system with Hawk trainer aircraft and a draft request for proposals is expected in 2014.

1 Including share of equity accounted investments.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 3).
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.
4 Order backlog comprises funded and unfunded unexecuted customer orders.

INTERIM MANAGEMENT REPORT CONTINUED
REPORTING SEGMENTS: PLATFORMS & SERVICES (US) CONTINUED

Under the Concepts and Operations for Space and Missile Defence Integration Capabilities contract, the business was awarded an $85m (£56m), two-year extension to continue its support of the US Army's Future Warfare Center, providing services for developing and understanding missile defence methods and technologies.

BAE Systems was awarded an $80m (£53m) contract to continue providing systems engineering and other technical services to support the operational readiness of US Navy submarine torpedoes and other weapons systems.

Land & Armaments
Portfolio streamlining activities continued during the period, with the sale of the Commercial Armored Vehicles business completed in February.

Vehicle Systems
Deliveries of upgraded Bradley fighting vehicles exceeded contractual targets during the first half of the year.

The proposal for the Paladin Integrated Management Low-Rate Initial Production contract was submitted in the first quarter, with contract award expected by the end of the year.

Work on the US Army's Ground Combat Vehicle programme continues under the $450m (£297m) technology development phase. The Hybrid Electric Drive system has successfully completed 2,000 miles of testing four months ahead of schedule. A contract modification to extend the technology development phase by six months has been received, with a ceiling price of $159m (£105m).

Work on the £0.5bn contract to upgrade and build CV90 vehicles for the Norwegian Army is on schedule, with the manufacture of new vehicles expected to begin in September.

As part of the Joint Light Tactical Vehicle industry team led by Lockheed Martin, the business has completed all 22 prototype vehicles being built during the engineering and manufacturing development phase.

In May, the business received a 90-day stop work order from the US government ceasing all integration work on Caiman Multi-Terrain Vehicles at its Sealy, Texas, facility.

The business expects a decision by the end of the year in the Close Combat Vehicle competition to deliver up to 138 infantry fighting vehicles to the Canadian Army.

A CV90 vehicle was delivered to the Danish Army in April to participate in a competitive evaluation to meet the requirement for up to 450 armoured personnel vehicles. An award decision is expected in the first quarter of 2014.

The business signed a teaming agreement in May with Polish Defence Holdings to offer a new family of armoured vehicles based on CV90 technology for Poland's Modular Tracked Platform requirement.

Weapons Systems & Support
In April, the business received a contract worth approximately $57m (£38m) for six 57mm Mk 3 naval guns for the Royal Malaysian Navy.

The business received a $40m (£26m) contract to produce vertical launching system canisters for the US Navy. If all options under the contract are exercised, the total value could exceed $400m (£264m).

The business is near completion of the five-year, £206m transformation of the UK munitions facilities.

Looking forward

Efforts to reduce the US government's budget deficit are likely to impact all areas of government spend. Whilst legislation was passed in March to set defence funding levels for the remainder of the 2013 Fiscal Year, a Continuing Resolution for the 2014 Fiscal Year is likely and the impact of Sequestration remains uncertain.

Whilst potential cancellations and delays in new programmes could affect the business, Support Solutions may be able to offset the impact through additional opportunities to sustain and modernise existing platforms.

Land & Armaments continues to operate in a challenging market environment. Whilst the business continues its rationalisation and restructuring activities to drive cost reductions and operational efficiencies, it remains focused on growing international opportunities and investing to protect current programmes.

REPORTING SEGMENTS: PLATFORMS & SERVICES (UK)

Platforms & Services (UK), with 27,600 employees[1], comprises the Group's UK-based air, maritime and combat vehicle activities, and certain shared services activities.

	Six months ended 30 June 2013	Six months ended 30 June 2012	Year ended 31 December 2012
Sales[1]	**£3,192m**	£2,651m	£5,646m
Underlying EBITA[2]	**£384m**	£420m	£689m
Return on sales	**12.0%**	15.8%	12.2%
Cash (outflow)/inflow[3]	**£(415)m**	£243m	£1,719m
Funded order intake[1]	**£2,355m**	£3,501m	£8,077m
Order backlog[1]	**£20.4bn**	£19.5bn	£21.2bn

Financial performance

Sales[1] of £3.2bn increased by 18% on a like-for-like basis compared to 2012. Salam Typhoon aircraft deliveries have resumed with four acceptances in the period. In addition, there was a higher level of deliveries under the Indian Hawk contract.

The return on sales of 15.8% seen in the first half of 2012 benefited from the strong programme execution and risk reduction on the European Typhoon production and Type 45 destroyer contracts. There was also good margin performance in the first half of this year at 12.0% despite there being no profit recognition on the four Salam Typhoon aircraft deliveries.

As expected, the £0.4bn cash outflow[3] in the period reflects the consumption of customer advances on the Omani Typhoon and Hawk programme, the European Typhoon contract and the Saudi training aircraft contract. In addition, provisions are being utilised against costs incurred on rationalisation and on the Oman Offshore Patrol Vessel (OPV) programme. The Trinidad and Tobago termination settlement payment of £131m is included within the reported cash outflow.

Order backlog[1] reduced to £20.4bn on the trading of the European and Saudi Typhoon aircraft and Indian Hawks.

Operational performance

Military Air & Information

Deliveries of Typhoon Tranche 2 aircraft to the four European partner nations totalled 15 in the period. At the end of June, cumulative aircraft deliveries to the four nations were 184 of the contracted 236. A further six Tranche 3 front fuselage sub-assemblies were manufactured for the European partner nations in the first half of the year.

The business continues to support its UK and European customers' Typhoon and Tornado aircraft and their operational commitments through availability-based service contracts.

On the F-35 Lightning II programme, the business delivered a further nine production aircraft fuselage assemblies to Lockheed Martin during the period, completing deliveries on the fifth Low-Rate Initial Production (LRIP) contract. Production of fuselage assemblies for the sixth LRIP contract has commenced, with five delivered at the half year.

Support continues to be provided to users of Hawk trainer aircraft across the world. Deliveries of materials and equipment in support of licence production of the 57 Batch 2 aircraft by Hindustan Aeronautics Limited continue to schedule. Discussions continue following the proposal submitted for an additional 20 Hawk aircraft to India.

Initial mobilisation under the Omani Typhoon and Hawk aircraft contract has commenced.

Preparation has been made for the flight trials of the Unmanned Combat Air System demonstrator, Taranis, which is due to fly in the second half of the year.

Equipment deliveries continue to schedule on the Falcon secure deployable communication system programme for the British Army and Royal Air Force, which entered into service in the second half of 2012.

Maritime

In June, the aft island, the final section of the first of the Royal Navy's new aircraft carriers, the Queen Elizabeth, departed from the Clyde and arrived at Rosyth for assembly. Manufacture of the second ship, Prince of Wales, is well underway. As the business progresses through the assembly phase and plans for the integration and test phase, the Aircraft Carrier Alliance is reviewing the future commercial construct of the programme with the Ministry of Defence (MoD).

HMS Duncan, the sixth and final Type 45 destroyer, was accepted by the MoD in March. The Type 45 support contract met all ship deployment dates in the first half of the year.

Cumulative savings of £459m have been reported to the MoD against commitments made under the 15-year Terms of Business Agreement (ToBA), which is ahead of target.

Final payment in settlement with the Government of the Republic of Trinidad and Tobago, in respect of the cancelled OPV programme, was made in May. Following the agreement in December 2011 for the sale of the OPVs to the Brazilian Navy, the third and final ship was delivered on schedule in June.

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 3).
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.

INTERIM MANAGEMENT REPORT CONTINUED
REPORTING SEGMENTS: PLATFORMS & SERVICES (UK) CONTINUED

Interim acceptance of the first Khareef Class corvette for Oman was achieved in June. The second ship is scheduled for interim acceptance in the second half of the year, with the final ship scheduled for 2014.

The assessment phase contract for the Type 26 Global Combat Ship continues and is planned to complete by the end of 2014.

The warship support modernisation initiative contract, for delivery of services at Portsmouth Naval Base, was extended for one year in April. A new maritime support delivery framework is expected to replace the existing contract in the second half of the year.

The Advanced Radar Target Indication Situational Awareness Navigation (ARTISAN) 3-D radar programme continues towards full production, with the first of class now fitted to HMS Iron Duke, a Type 23 frigate.

HMS Astute, the first of class attack submarine for the Royal Navy, achieved operational handover in April and HMS Ambush, the second of class, achieved operational handover in June. The third of class, Artful, is planned to launch in 2014. A further £126m of long lead item orders were received on boats 6 and 7.

The design and development phase of the Successor submarine programme, to replace the Vanguard Class fleet, continues. Over 1,100 people are now employed on this programme.

Combat Vehicles (UK)
The Terrier combat engineer vehicle was declared ‘in service’ by the MoD in April, with 20 of the 60 contracted vehicles delivered. Final vehicle deliveries are expected during the first half of 2014.

Looking forward

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

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

In Maritime, sales are underpinned by the Queen Elizabeth Class carrier and Astute Class submarine manufacturing programmes, the 15-year ToBA, the warship support modernisation initiative contract, and the design of the Successor submarine and Type 26. The through-life support of these platforms and Type 45, together with their associated command and combat systems, provides sustainable business in technical services and mid-life upgrades. Discussions continue with the MoD to balance naval surface shipbuilding capacity in the UK with future warship demand in accordance with the ToBA.

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

REPORTING SEGMENTS: PLATFORMS & SERVICES (INTERNATIONAL)

Platforms & Services (International), with 15,200 employees[1], comprises the Group's businesses in Saudi Arabia, Australia, India and Oman, together with its 37.5% interest in the pan-European MBDA joint venture.

	Six months ended 30 June 2013	Six months ended 30 June 2012	Year ended 31 December 2012
Sales[1]	**£1,654m**	£1,573m	£4,071m
Underlying EBITA[2]	**£165m**	£161m	£417m
Return on sales	**10.0%**	10.2%	10.2%
Cash (outflow)/inflow[3]	**£(221)m**	£568m	£506m
Funded order intake[1]	**£4,178m**	£1,512m	£5,266m
Order backlog[1]	**£11.9bn**	£8.1bn	£9.3bn

Financial performance

Sales[1] for the first six months of £1.7bn are 5% higher than in 2012. The increase is primarily on the increased levels of support to Typhoon aircraft now in service.

Underlying EBITA[2] was £165m and the return on sales in the first half of 10.0% is broadly consistent with last year and in line with guidance.

There was an operating cash outflow[3] of £221m as 2012's accelerated receipts on the Saudi Tornado upgrade programme were utilised and in Australia where advances were consumed on the Landing Helicopter Dock contract.

Order backlog[1] has increased to £11.9bn following awards for the five-year Typhoon follow-on support contract and further weapons package in Saudi Arabia, together with renewal of the Australian Hawk support programme.

Operational performance

Saudi Arabia

On the Salam Typhoon programme, aircraft deliveries re-commenced in April, with four delivered to the Royal Saudi Air Force (RSAF) in the first half of 2013. To date, 28 of the 72 aircraft contracted have been delivered and a further six are planned to be delivered by year end. Work to expand the multi-role capabilities of the aircraft continues to progress to schedule. A £1.8bn order for follow-on support covering the five-year period to the end of 2017 was received in June.

Conclusion of discussions with the Saudi Arabian government on price escalation under the Salam Typhoon programme has not yet been reached.

A £0.3bn contract was signed in March for the construction of airfield facilities at King Fahd Air Base in Saudi Arabia. Discussions on the provision of maintenance and upgrade facilities in-Kingdom, and further capability enhancement of the Typhoon aircraft remain ongoing.

Under an order received at the end of 2012 to deliver training to the RSAF, the first graduation ceremony of cadets from the King Faisal Air Academy was held in May.

Following the completion of upgrades to the RSAF Tornado fleet in 2012 under the Tornado Sustainment Programme (TSP), discussions have commenced regarding further capability enhancements expected to be contracted during the second half of 2013.

Under the TSP, further Storm Shadow missiles were delivered in the first half of 2013, with final deliveries due by the end of the year. A follow-on £0.6bn weapons contract was awarded in March, with deliveries expected to commence in 2014.

Work continues on the first ship re-fit on the minehunter mid-life update programme, with hand back to the Royal Saudi Naval Forces due in the second half of 2013.

On the C4i[5] programme, the business continues to seek an acceptable resolution to the closure of the contract.

Australia

The Australian government issued a Defence White Paper in May which, together with accompanying government communications, has confirmed the reallocation of four Air Warfare Destroyer (AWD) blocks to the Williamstown shipyard, the replacement of the Royal Australian Navy's replenishment vessels through a competitive tender and affirmed a commitment to the implementation of the Future Submarine Industry Skills Plan.

The superstructure and hull for the first Landing Helicopter Dock were consolidated at the Williamstown shipyard, with integration of the ship's combat and communications systems continuing.

All 11 hull blocks for the AWD programme under the A$200m (£121m) subcontract have been constructed and accepted by the customer, with nine delivered and additional scope of work being performed on two. An A$44m (£27m) order for four additional blocks was received in the period.

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 3).
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.
5 Command, Control, Communications, Computers and Intelligence.

INTERIM MANAGEMENT REPORT CONTINUED
REPORTING SEGMENTS: PLATFORMS & SERVICES (INTERNATIONAL) CONTINUED

Upgrade of the second Royal Australian Navy ANZAC Class frigate with a new anti-ship missile defence capability has commenced at the Henderson shipyard. An additional A$64m (£39m) contract was received during the period to perform engineering changes across the ANZAC fleet.

The business secured the Hawk Lead-In Fighter in-service support contract valued at A$342m (£206m) for a further five years and won an A$107m (£65m), five-year contract to deliver the Australian Defence Force's aviation technical training.

The business was not down-selected for the Land Materiel Maintenance element of the Defence Logistics Transformation Programme, although it remains under consideration for the A$0.5bn (£0.3bn) Warehousing and Distribution element.

India

BAE Systems sold its 26% shareholding in Defence Land Systems India to Mahindra & Mahindra, the holder of the other 74% of the shares in the joint venture.

The US government has issued a Letter of Acceptance to the Indian government under the US Foreign Military Sales process for the supply of 145 M777 howitzers for the Indian Army. This is expected to be ratified by the Indian government in the second half of the year.

A proposal has been submitted to Hindustan Aeronautics Limited (HAL) for the third batch of Hawk trainer aircraft for the Indian Air Force and discussions with the customer continue.

Whilst the Indian government deemed Dassault to be the lowest priced compliant bidder in the Medium Multi-Role Combat Aircraft competition, contract negotiations that began in early 2012 have not been concluded. The Group continues to monitor the competition and stands ready to support the Indian government's procurement process.

MBDA

Continued progress has been made on the Team Complex Weapons business arrangements in the UK. In France, the publication of the Livre Blanc confirmed the intention to launch a number of new missile development programmes of significance to MBDA. The US has confirmed its continued commitment to the development phase of the tri-national MEADS programme, alongside Germany and Italy. The recently secured German Meteor production order completes the production commitment of the six partner nations.

In export markets, a follow-on production order for the ASTER system was secured, together with orders for airborne systems from a Middle Eastern customer. In India, the Advanced Short Range Air-to-Air Missile (ASRAAM) has been down-selected and negotiations on the Maitri surface-to-air missile concluded, with final procurement decisions on both programmes awaited.

Looking forward

In the Kingdom of Saudi Arabia, the Group will continue to progress the Salam price escalation discussions and look to grow order backlog through the capability upgrades identified on both the Typhoon and Tornado platforms. Following receipt of the order for the second phase of Salam support, the focus is now on mobilisation activities and programme delivery.

In Australia, the Group will continue to work with the Department of Defence to sustain the necessary shipbuilding skills for future naval programmes and to deliver cost and service improvements across all sectors.

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

In MBDA, the focus is on securing a pipeline of domestic opportunities and growth from export markets, potentially benefiting from significant military aircraft procurements.

RESPONSIBILITY STATEMENT OF THE DIRECTORS IN RESPECT OF THE HALF-YEARLY FINANCIAL REPORT

Each of the directors (as detailed opposite) confirms that to the best of his/her knowledge:

– The condensed set of financial statements has been prepared in accordance with IAS 34, Interim Financial Reporting, as adopted by the European Union.

– The interim management report includes a fair review of the information required by:

(a) DTR 4.2.7R of the Disclosure and Transparency Rules (DTR), being an indication of important events that have occurred during the first six months of the financial year and their impact on the condensed set of financial statements; and a description of the principal risks and uncertainties for the remaining six months of the year; and

(b) DTR 4.2.8R of the DTR, being related party transactions that have taken place in the first six months of the current financial year and that have materially affected the financial position or performance of the Company during that period; and any changes in the related party transactions described in the last annual report that could do so.

For and on behalf of the directors:

Sir Richard Olver
Chairman

31 July 2013

Directors

Sir Richard Olver	Chairman
Ian King	Chief Executive
Linda Hudson	President and Chief Executive Officer of BAE Systems, Inc.
Peter Lynas	Group Finance Director
Paul Anderson	Non-executive director
Harriet Green	Non-executive director
Chris Grigg	Non-executive director
Lee McIntire	Non-executive director
Paula Rosput Reynolds	Non-executive director
Nick Rose	Non-executive director
Carl Symon	Non-executive director
Ian Tyler	Non-executive director

INDEPENDENT REVIEW REPORT TO BAE SYSTEMS PLC

Introduction
We have been engaged by the Company to review the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2013 which comprises the Condensed Consolidated Income Statement, the Condensed Consolidated Statement of Comprehensive Income, the Condensed Consolidated Cash Flow Statement, the Condensed Consolidated Balance Sheet, the Condensed Consolidated Statement of Changes in Equity and the related explanatory notes. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with the terms of our engagement to assist the Company in meeting the requirements of the Disclosure and Transparency Rules (the DTR) of the UK's Financial Conduct Authority (the UK FCA). Our review has been undertaken so that we might state to the Company those matters we are required to state to it in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company for our review work, for this report, or for the conclusions we have reached.

Directors' responsibilities
The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the DTR of the UK FCA.

The annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union (EU). The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with IAS 34, Interim Financial Reporting, as adopted by the EU.

Our responsibility
Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

Scope of review
We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 Review of Interim Financial Information Performed by the Independent Auditor of the Entity issued by the Auditing Practices Board for use in the UK. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (UK and Ireland) and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion
Based on our review, nothing has come to our attention that causes us to believe that the condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2013 is not prepared, in all material respects, in accordance with IAS 34 as adopted by the EU and the DTR of the UK FSA.

Ian Starkey
for and on behalf of KPMG Audit Plc
Chartered Accountants
15 Canada Square
London E14 5GL

31 July 2013

CONDENSED CONSOLIDATED INCOME STATEMENT

	Notes	Six months ended 30 June 2013 £m	Six months ended 30 June 2013 £m	Restated[1] Six months ended 30 June 2012 £m	Restated[1] Six months ended 30 June 2012 £m
Continuing operations					
Combined sales of Group and share of equity accounted investments	2		**8,448**		8,334
Less: share of sales of equity accounted investments	2		**(496)**		(497)
Revenue	2		**7,952**		7,837
Operating costs			**(7,301)**		(7,212)
Other income			**55**		120
Group operating profit			**706**		745
Share of results of equity accounted investments			**44**		23
Underlying EBITA[2]		**865**		922	
Non-recurring items[3]		**4**		18	
EBITA		**869**		940	
Amortisation		**(96)**		(101)	
Impairment		**(4)**		(63)	
Financial (expense)/income of equity accounted investments	3	**(2)**		1	
Taxation expense of equity accounted investments		**(17)**		(9)	
Operating profit	2		**750**		768
Financial income		**278**		164	
Financial expense		**(499)**		(357)	
Finance costs	3		**(221)**		(193)
Profit before taxation			**529**		575
Taxation expense			**(116)**		(152)
Profit for the period – continuing operations			**413**		423
Profit for the period – discontinued operations			**2**		4
Profit for the period			**415**		427
Attributable to:					
Equity shareholders			**411**		419
Non-controlling interests			**4**		8
			415		427
Earnings per share	4				
Basic earnings per share			**12.7p**		12.9p
Diluted earnings per share			**12.6p**		12.9p
Earnings per share – continuing operations	4				
Basic earnings per share			**12.6p**		12.8p
Diluted earnings per share			**12.5p**		12.8p

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3 Non-recurring items includes profit on disposal of businesses £4m (2012 £18m).

CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Six months ended 30 June 2013			Restated[1] Six months ended 30 June 2012		
	Other reserves £m	Retained earnings £m	Total £m	Other reserves £m	Retained earnings £m	Total £m
Profit for the period	–	415	415	–	427	427
Other comprehensive income						
Items that will not be reclassified to the income statement:						
Remeasurements on defined benefit pension schemes:						
Subsidiaries	–	282	282	–	(605)	(605)
Equity accounted investments	–	(16)	(16)	–	(25)	(25)
Tax on items that will not be reclassified to the income statement[2]	–	(133)	(133)	–	145	145
Items that may be reclassified to the income statement:						
Currency translation on foreign currency net investments:						
Subsidiaries	307	–	307	(43)	–	(43)
Equity accounted investments	11	–	11	(21)	–	(21)
Reclassification of cumulative currency translation reserve on disposal	(8)	–	(8)	(13)	–	(13)
Amounts credited/(charged) to hedging reserve	69	–	69	(34)	–	(34)
Tax on items that may be reclassified to the income statement	(16)	–	(16)	11	–	11
Total other comprehensive income for the period (net of tax)	363	133	496	(100)	(485)	(585)
Total comprehensive income for the period	363	548	911	(100)	(58)	(158)
Attributable to:						
Equity shareholders	364	544	908	(100)	(66)	(166)
Non-controlling interests	(1)	4	3	–	8	8
	363	548	911	(100)	(58)	(158)

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.
2 Included within the credit of £145m in 2012 is a charge of £38m arising on the reduction of the UK current tax rate from 26% to 24% with effect from 1 April 2012.

NOTES TO THE CONDENSED HALF-YEARLY FINANCIAL STATEMENTS

1. Preparation

Basis of preparation and statement of compliance

These condensed consolidated half-yearly financial statements of BAE Systems plc (the Group) have been prepared in accordance with International Accounting Standard (IAS) 34, Interim Financial Reporting. The annual consolidated financial statements of the Group are prepared in accordance with EU-endorsed International Financial Reporting Standards (IFRSs). These condensed consolidated half-yearly financial statements do not comprise statutory accounts within the meaning of Section 435 of the Companies Act 2006, and should be read in conjunction with the Annual Report 2012. The comparative figures for the year ended 31 December 2012 are not the Group's statutory accounts for that financial year. Those accounts have been reported upon by the Group's auditors and delivered to the registrar of companies. The report of the auditors was unqualified, did not include a reference to any matters to which the auditors drew attention by way of emphasis without qualifying their report and did not contain statements under Section 498 (2) or (3) of the Companies Act 2006.

Except as described below, the accounting policies adopted in the preparation of these condensed consolidated half-yearly financial statements to 30 June 2013 are consistent with the accounting policies applied by the Group in its consolidated financial statements as at, and for the year ended, 31 December 2012 as required by the Disclosure and Transparency Rules of the UK's Financial Services Authority.

Changes in accounting policies

With effect from 1 January 2013, the Group has adopted the following new standard and amendment to an existing standard:

– IAS 19 (revised 2011), Employee Benefits, replaces interest cost and expected return on plan assets with a finance cost on the pension deficit. The finance cost is calculated using the rate currently used to discount defined benefit pension liabilities. The discount rate is lower than the expected return on plan assets, increasing finance costs recognised in the income statement and correspondingly reducing remeasurements recognised in other comprehensive income. In addition, certain costs associated with the administration of the Group's pension schemes are now reported within operating costs rather than finance costs. The net pension deficit is unchanged.

  These changes have been applied retrospectively to the comparative financial information for 2012 and have had the following impact on the financial statements compared with the previous version of IAS 19:

	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m
Operating costs	**(15)**	(17)
Share of results of equity accounted investments	**(1)**	(1)
Finance costs	**(102)**	(62)
Profit before taxation	**(118)**	(80)
Taxation expense	**35**	25
Net decrease in profit for the period	**(83)**	(55)
Remeasurements on defined benefit pension schemes	**118**	80
Tax on items that will not be reclassified to the income statement	**(35)**	(25)
Total comprehensive income for the period	**–**	–
Earnings per share		
Basic earnings per share	**(2.6)p**	(1.7)p
Diluted earnings per share	**(2.6)p**	(1.7)p
Underlying earnings[1] per share – continuing operations		
Underlying earnings[1] per share	**(0.1)p**	(0.2)p

  The reduction in underlying earnings[1] per share mainly reflects the reclassification of certain costs associated with the administration of the Group's pension schemes from finance movements on pensions, which are excluded from underlying earnings[1], to underlying EBITA[2].

– IFRS 13, Fair Value Measurement, aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement disclosure requirements for use across other standards within IFRSs. IFRS 13 does not extend the use of fair value accounting and has not impacted the fair value measurements carried out by the Group. IFRS 13 requires specific disclosures on fair values, some of which are required by IAS 34 and provided in note 7.

There are no other new standards, amendments to existing standards or IFRIC interpretations that are effective that have had an impact on the Group.

1 Earnings excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items (see note 4).
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items (see page 3).

NOTES TO THE CONDENSED HALF-YEARLY FINANCIAL STATEMENTS – CONDENSED CONSOLIDATED INCOME STATEMENT

2. Segmental analysis

Sales and revenue by reporting segment

	Combined sales of Group and share of equity accounted investments		Less: sales by equity accounted investments		Add: sales to equity accounted investments		Revenue	
	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m
Electronic Systems	**1,194**	1,181	**(30)**	(26)	**30**	26	**1,194**	1,181
Cyber & Intelligence	**657**	714	**–**	–	**–**	–	**657**	714
Platforms & Services (US)	**2,085**	2,254	**(35)**	(23)	**–**	–	**2,050**	2,231
Platforms & Services (UK)	**3,192**	2,651	**(517)**	(736)	**484**	709	**3,159**	2,624
Platforms & Services (International)	**1,654**	1,573	**(297)**	(337)	**–**	–	**1,357**	1,236
HQ	**145**	123	**(145)**	(123)	**–**	–	**–**	–
	8,927	8,496	**(1,024)**	(1,245)	**514**	735	**8,417**	7,986
Intra-group sales/revenue	**(479)**	(162)	**–**	–	**14**	13	**(465)**	(149)
	8,448	8,334	**(1,024)**	(1,245)	**528**	748	**7,952**	7,837

Reporting segment result

	Underlying EBITA[2]		Non-recurring items[3]		Amortisation of intangible assets		Impairment of intangible assets		Reporting segment result	
		Restated[1]								Restated[1]
	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m	**Six months ended 30 June 2013 £m**	Six months ended 30 June 2012 £m
Electronic Systems	**156**	164	**–**	–	**(7)**	(9)	**(4)**	(2)	**145**	153
Cyber & Intelligence	**53**	54	**–**	–	**(29)**	(26)	**–**	–	**24**	28
Platforms & Services (US)	**182**	189	**5**	18	**(12)**	(48)	**–**	(61)	**175**	98
Platforms & Services (UK)	**384**	420	**–**	–	**(45)**	(14)	**–**	–	**339**	406
Platforms & Services (International)	**165**	161	**(1)**	–	**(3)**	(4)	**–**	–	**161**	157
HQ	**(75)**	(66)	**–**	–	**–**	–	**–**	–	**(75)**	(66)
	865	922	**4**	18	**(96)**	(101)	**(4)**	(63)	**769**	776
Financial (expense)/income of equity accounted investments									**(2)**	1
Taxation expense of equity accounted investments									**(17)**	(9)
Operating profit									**750**	768
Finance costs									**(221)**	(193)
Profit before taxation									**529**	575
Taxation expense									**(116)**	(152)
Profit for the period – continuing operations									**413**	423

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.
2 Earnings before amortisation and impairment of intangible assets, finance costs and taxation expense (EBITA) excluding non-recurring items.
3 Non-recurring items includes profit on disposal of businesses £4m (2012 £18m).

NOTES TO THE CONDENSED HALF-YEARLY FINANCIAL STATEMENTS – CONDENSED CONSOLIDATED INCOME STATEMENT CONTINUED

3. Finance costs

	Six months ended 30 June 2013 £m	Restated[1] Six months ended 30 June 2012 £m
Finance costs:		
Group	**(221)**	(193)
Share of equity accounted investments	**(2)**	1
	(223)	(192)
Analysed as:		
Underlying interest (expense)/income:		
Group	**(98)**	(98)
Share of equity accounted investments	**3**	7
	(95)	(91)
Other:		
Group:		
Net interest expense on retirement benefit obligations	**(98)**	(95)
Fair value and foreign exchange adjustments on financial instruments and investments	**(25)**	–
Share of equity accounted investments	**(5)**	(6)
	(223)	(192)

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.

4. Earnings per share

	Six months ended 30 June 2013			Restated[1] Six months ended 30 June 2012		
	£m	**Basic pence per share**	**Diluted pence per share**	£m	Basic pence per share	Diluted pence per share
Profit for the period attributable to equity shareholders	**411**	**12.7**	**12.6**	419	12.9	12.9
Represented by:						
Continuing operations	**409**	**12.6**	**12.5**	415	12.8	12.8
Discontinued operations	**2**	**0.1**	**0.1**	4	0.1	0.1
(Deduct)/add back:						
Profit on disposal of businesses	**(4)**			(18)		
Net interest expense on retirement benefit obligations, post tax	**78**			72		
Fair value and foreign exchange adjustments on financial instruments and investments, post tax	**19**			2		
Amortisation and impairment of intangible assets, post tax	**75**			92		
Impairment of goodwill	**–**			39		
Underlying earnings, post tax	**579**	**17.9**	**17.8**	606	18.7	18.6
Represented by:						
Continuing operations	**577**	**17.8**	**17.7**	602	18.6	18.5
Discontinued operations	**2**	**0.1**	**0.1**	4	0.1	0.1
	579	**17.9**	**17.8**	606	18.7	18.6
		Millions	**Millions**		Millions	Millions
Weighted average number of shares used in calculating basic earnings per share		**3,243**	**3,243**		3,240	3,240
Incremental shares in respect of employee share schemes			**10**			9
Weighted average number of shares used in calculating diluted earnings per share			**3,253**			3,249

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.

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.

CONDENSED CONSOLIDATED CASH FLOW STATEMENT

	Notes	Six months ended 30 June 2013 £m	Restated[1] Six months ended 30 June 2012 £m
Profit for the period		**415**	427
Taxation expense		**116**	152
Share of results of equity accounted investments		**(44)**	(23)
Finance costs		**221**	193
Depreciation, amortisation and impairment		**255**	320
Loss/(profit) on disposal of property, plant and equipment		**5**	(3)
Profit on disposal of investment property		**(6)**	(3)
Profit on disposal of businesses		**(4)**	(19)
Cost of equity-settled employee share schemes		**26**	28
Movements in provisions		**(34)**	(143)
Decrease in liabilities for retirement benefit obligations		**(147)**	(186)
(Increase)/decrease in working capital:			
Inventories		**(59)**	(110)
Trade and other receivables		**(443)**	(147)
Trade and other payables		**(1,029)**	424
Cash (outflow)/inflow from operating activities[2]		**(728)**	910
Interest paid		**(88)**	(99)
Taxation paid		**(94)**	(56)
Net cash (outflow)/inflow from operating activities		**(910)**	755
Dividends received from equity accounted investments		**10**	16
Interest received		**7**	31
Purchases of property, plant and equipment, and investment property		**(105)**	(173)
Purchases of intangible assets		**(11)**	(25)
Proceeds from sale of property, plant and equipment, and investment property		**20**	9
Purchase of subsidiary undertakings (net of cash acquired)		**(1)**	(5)
Equity accounted investment funding		**(1)**	–
Proceeds from sale of subsidiary undertakings (net of cash disposed)		**7**	23
Net cash outflow from investing activities		**(74)**	(124)
Net purchase of own shares		**(90)**	(16)
Equity dividends paid	6	**(380)**	(367)
Dividends paid to non-controlling interests		**(12)**	(11)
Cash inflow/(outflow) from matured derivative financial instruments		**33**	(49)
Movement in cash collateral		**2**	–
Cash inflow from loans		**–**	1,457
Cash outflow from repayment of loans		**–**	(1,326)
Net cash outflow from financing activities		**(447)**	(312)
Net (decrease)/increase in cash and cash equivalents		**(1,431)**	319
Cash and cash equivalents at 1 January		**3,334**	2,136
Effect of foreign exchange rate changes on cash and cash equivalents		**7**	(4)
Cash and cash equivalents at end of period		**1,910**	2,451
Comprising:			
Cash and cash equivalents[3]		**1,919**	2,464
Overdrafts		**(9)**	(13)
Cash and cash equivalents at end of period		**1,910**	2,451

1 On adoption of the revised International Accounting Standard 19, Employee Benefits.
2 See reconciliation to operating business cash flow on page 4.
3 At 30 June 2012, included £428m of cash held in Trust for the benefit of the BAE Systems Pension Scheme and BAE Systems 2000 Pension Plan.

CONDENSED CONSOLIDATED BALANCE SHEET

	Notes	30 June 2013 £m	31 December 2012 £m
Non-current assets			
Intangible assets		**11,218**	10,928
Property, plant and equipment		**2,272**	2,285
Investment property		**142**	122
Equity accounted investments		**294**	265
Other investments		**5**	5
Other receivables		**299**	254
Other financial assets		**101**	62
Deferred tax assets		**1,202**	1,375
		15,533	15,296
Current assets			
Inventories		**738**	655
Trade and other receivables including amounts due from customers for contract work		**3,392**	2,873
Current tax		**44**	11
Other financial assets		**91**	64
Cash and cash equivalents		**1,919**	3,355
Assets held for sale		**21**	20
		6,205	6,978
Total assets		**21,738**	22,274
Non-current liabilities			
Loans		**(2,809)**	(2,967)
Trade and other payables		**(1,336)**	(1,481)
Retirement benefit obligations	5	**(4,338)**	(4,607)
Other financial liabilities		**(54)**	(66)
Deferred tax liabilities		**(7)**	(13)
Provisions		**(510)**	(449)
		(9,054)	(9,583)
Current liabilities			
Loans and overdrafts		**(338)**	(21)
Trade and other payables		**(7,334)**	(8,067)
Other financial liabilities		**(81)**	(88)
Current tax		**(443)**	(422)
Provisions		**(237)**	(297)
Liabilities held for sale		**(25)**	(22)
		(8,458)	(8,917)
Total liabilities		**(17,512)**	(18,500)
Net assets		**4,226**	3,774
Capital and reserves			
Issued share capital		**89**	90
Share premium		**1,249**	1,249
Other reserves		**5,444**	5,079
Retained earnings – deficit		**(2,601)**	(2,698)
Total equity attributable to equity holders of the parent		**4,181**	3,720
Non-controlling interests		**45**	54
Total equity		**4,226**	3,774

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to equity holders of the parent						
	Issued share capital £m	Share premium £m	Other reserves[1] £m	Retained earnings £m	Total £m	Non-controlling interests £m	Total equity £m
At 1 January 2013	90	1,249	5,079	(2,698)	3,720	54	3,774
Profit for the period	–	–	–	411	411	4	415
Total other comprehensive income for the period	–	–	364	133	497	(1)	496
Share-based payments	–	–	–	26	26	–	26
Net purchase of own shares	(1)	–	1	(93)	(93)	–	(93)
Ordinary share dividends	–	–	–	(380)	(380)	(12)	(392)
At 30 June 2013	**89**	**1,249**	**5,444**	**(2,601)**	**4,181**	**45**	**4,226**
At 1 January 2012	90	1,249	5,381	(2,480)	4,240	59	4,299
Profit for the period[2]	–	–	–	419	419	8	427
Total other comprehensive income for the period[2]	–	–	(100)	(485)	(585)	–	(585)
Share-based payments	–	–	–	28	28	–	28
Net purchase of own shares	–	–	–	(16)	(16)	–	(16)
Ordinary share dividends	–	–	–	(367)	(367)	(11)	(378)
Other	–	–	–	–	–	(1)	(1)
At 30 June 2012	90	1,249	5,281	(2,901)	3,719	55	3,774

1 The net increase comprises translation reserve £311m (2012 decrease £77m), hedging reserve £53m (2012 decrease £23m) and capital redemption reserve £1m (2012 £nil).

2 Restated on adoption of the revised International Accounting Standard 19, Employee Benefits.

NOTES TO THE CONDENSED HALF-YEARLY FINANCIAL STATEMENTS – CONDENSED CONSOLIDATED BALANCE SHEET

5. Retirement benefit obligations

	UK £m	US and other £m	Total £m
Total IAS 19 deficit at 1 January 2013	(4,795)	(913)	(5,708)
Actual return on assets excluding amounts included in interest expense	442	28	470
(Increase)/decrease in liabilities due to changes in assumptions and experience	(659)	373	(286)
Additional contributions in excess of service cost	161	–	161
Recurring contributions above/(below) service cost	37	(6)	31
Past service cost – plan amendments	(7)	–	(7)
Net interest expense	(103)	(19)	(122)
Foreign exchange adjustments	–	(56)	(56)
Movement in US healthcare schemes	–	17	17
Total IAS 19 deficit at 30 June 2013	**(4,924)**	**(576)**	**(5,500)**
Allocated to equity accounted investments and other participating employers	1,213	–	1,213
Group's share of IAS 19 deficit excluding Group's share of amounts allocated to equity accounted investments and other participating employers at 30 June 2013	**(3,711)**	**(576)**	**(4,287)**
Represented by:			
Pension prepayments (within other receivables)	–	51	51
Retirement benefit obligations	(3,711)	(627)	(4,338)
	(3,711)	**(576)**	**(4,287)**

The net increase in liabilities due to changes in assumptions and experience reflects, in the UK, a 0.3 percentage point reduction in the real discount rate to 1.3% and, in the US, a 0.8 percentage point increase in the nominal discount rate to 4.9%.

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

The pension deficit is £3.2bn (31 December 2012 £3.4bn) after tax.

NOTES TO THE CONDENSED HALF-YEARLY FINANCIAL STATEMENTS – OTHER INFORMATION

6. Equity dividends

	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m
Prior year final 11.7p dividend per ordinary share paid in the period (2012 11.3p)	**380**	367

The directors have declared an interim dividend of 8.0p per ordinary share (2012 7.8p), totalling £259m (2012 £253m). The dividend will be paid on 2 December 2013 to shareholders registered on 25 October 2013. The ex-dividend date is 23 October 2013.

Shareholders who do not at present participate in the Company's Dividend Reinvestment Plan and wish to receive the final dividend in shares rather than cash should complete a mandate form for the Dividend Reinvestment Plan and return it to the registrars no later than 11 November 2013.

7. Fair value measurement

Fair value of financial instruments

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the balance sheet date.

The fair values of financial instruments held at fair value have been determined based on available market information at the balance sheet date and the valuation methodologies listed below:

- the fair values of forward foreign exchange contracts are calculated by discounting the contracted forward values and translating at the appropriate balance sheet rates;
- the fair values of both interest rate and cross-currency swaps are calculated by discounting expected future principal and interest cash flows and translating at the appropriate balance sheet rates; and
- the fair values of loans have been estimated by discounting the future cash flows to net present values using appropriate market-based interest rates prevailing at the balance sheet date.

Carrying values and fair values of certain financial assets and liabilities

	30 June 2013		31 December 2012	
Carrying values	Assets £m	Liabilities £m	Assets £m	Liabilities £m
Non-current				
Available-for-sale financial assets	**5**	**–**	5	–
Other financial assets	**101**	**–**	62	–
Loans	**–**	**(2,809)**	–	(2,967)
Other financial liabilities	**–**	**(54)**	–	(66)
Current				
Other financial assets	**91**	**–**	64	–
Cash and cash equivalents	**1,919**	**–**	3,355	–
Loans	**–**	**(329)**	–	–
Overdrafts	**–**	**(9)**	–	(21)
Other financial liabilities	**–**	**(81)**	–	(88)

Financial assets and liabilities in the Group's consolidated balance sheet are either held at fair value or the carrying value approximates to fair value, with the exception of loans, most of which are held at amortised cost.

The fair value of total loans estimated using market prices at 30 June 2013 is £3,477m (31 December 2012 £3,407m).

Fair value hierarchy

All of the financial assets and liabilities above held at fair value are classified as level 2 using the fair value hierarchy described on page 148 of the Annual Report 2012. There were no transfers between levels during the period.

NOTES TO THE CONDENSED HALF-YEARLY FINANCIAL STATEMENTS – OTHER INFORMATION CONTINUED

8. Related party transactions

Transactions with related parties are shown on page 169 of the Annual Report 2012. The more significant transactions in the period are disclosed below:

	Six months ended 30 June 2013 £m	Six months ended 30 June 2012 £m
Sales to equity accounted investments	**528**	748
Purchases from equity accounted investments	**55**	53

	30 June 2013 £m	31 December 2012 £m
Amounts owed by equity accounted investments	**206**	163
Amounts owed to equity accounted investments	**604**	708

9. Contingent liability

Since 2009, BAE Systems, Inc. has been in dispute with a customer, AM General LLC. On 2 April 2013, the Superior Court in Gary, Indiana, USA, issued a ruling in favour of AM General's claim, denying a counterclaim from BAE Systems, Inc. and entering judgement against BAE Systems, Inc. which, including interest, amounted to $272m (£179m). Having considered the judgement, BAE Systems, Inc. has instructed its lawyers to continue to defend vigorously the claim and to pursue the counterclaim through all available judicial means.

10. Annual General Meeting

The Annual General Meeting of BAE Systems plc will be held on 7 May 2014.

FOR MORE INFORMATION

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