BAE Systems plc
Preliminary Announcement 2018

Results in brief

Financial performance measures as defined by the Group[1]

	2018	2017 (restated[3])
Order intake[4]	**£28,280m**	£20,257m
Order backlog[4]	**£48.4bn**	£38.7bn
Sales	**£18,407m**	£18,487m
Underlying EBITA	**£1,928m**	£1,974m
Underlying earnings per share	**42.9p**	42.1p
Operating business cash flow	**£993m**	£1,752m
Net debt	**£(904)m**	£(752)m

Financial performance measures defined in IFRS[2]

	2018	2017 (restated[3])
Revenue	**£16,821m**	£17,224m
Operating profit	**£1,605m**	£1,419m
Basic earnings per share	**31.3p**	26.0p
Net cash flow from operating activities	**£1,200m**	£1,897m

Other financial highlights

	2018	2017 (restated[3])
Group's share of the net pension deficit	**£(3.9)bn**	£(4.0)bn
Dividend per share	**22.2p**	21.8p

Charles Woodburn, Chief Executive, said: "*The Group made good progress in strengthening the outlook and geographic base of the business, with a number of significant contract wins. The defence order backlog is now at a record high with visibility on many of our key programmes through the next decade. Delivering a strong operational performance and continued investment will enable us to meet our growth expectations and underpin the long term.*"

Financial highlights

Financial performance measures as defined by the Group[1]

- Order intake increased by £8.0bn to £28.3bn.
- Order backlog increased by £9.7bn to £48.4bn following this year's record order intake.
- Sales decreased £0.1bn to £18.4bn with the expected reduction in Typhoon production activity being largely offset by growth in our US businesses.
- Underlying EBITA decreased by £46m to £1,928m. There was an adverse exchange translation impact of £34m.
- Underlying earnings per share increased by 2% to 42.9p.
- Operating business cash flow decreased by £759m to £993m.
- Net debt increased by £152m compared with 31 December 2017.

Financial performance measures defined in IFRS[2]

- Revenue decreased by £0.4bn to £16.8bn, a 1% decline on a constant currency basis[5].
- Operating profit increased by £186m to £1,605m. There was an adverse exchange translation impact of £31m.
- Basic earnings per share increased to 31.3p.
- Net cash flow from operating activities decreased by £697m to £1,200m.

Other financial highlights

- Group's share of the pre-tax accounting net pension deficit reduced by £0.1bn compared with 31 December 2017 to £3.9bn.
- Final dividend of 13.2p per share making a total of 22.2p per share for the year, an increase of 2% over 2017.

1. We monitor the underlying financial performance of the Group using alternative performance measures. These measures are not defined in International Financial Reporting Standards (IFRS) and, therefore, are considered to be non-GAAP (Generally Accepted Accounting Principles) measures. Accordingly, the relevant IFRS measures are also presented where appropriate. For alternative performance measure definitions see glossary on page 12.
2. International Financial Reporting Standards.
3. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers and to correct a prior year error in respect of the accounting valuation of a longevity swap held by one of the Group's defined benefit pension schemes. See note 11 for details regarding the restatement.
4. Including share of equity accounted investments.
5. Current year compared with prior year translated at current year exchange rates.

Operational and strategic key points

Air

- Contract with the Qatar government for the supply of 24 Typhoon and nine Hawk aircraft, air and ground training, and ground support became effective in September. MBDA contract for the supply of missiles also became effective
- Signature in March 2018 of a Memorandum of Intent between the Kingdom of Saudi Arabia and the UK government to aim to finalise discussions for the purchase of a further 48 Typhoon aircraft
- RAF declaration of Typhoon Centurion standard, enabling transition of capabilities from Tornado to Typhoon
- Announcement of the UK Combat Air Strategy and launch of the Tempest programme
- Completion of the final four of 12 Typhoon deliveries to Oman
- In November the first flight of a Hawk assembled in Saudi Arabia took place
- Integration of F-35 Lightning II onto aircraft carrier HMS Queen Elizabeth commenced, and the first F-35 deck landing completed
- Order intake of £3.2bn for support services up to 2022 in respect of the continuation of Typhoon support in Saudi Arabia
- Current German government position on export licensing may affect the Group's ability to provide capability to Saudi Arabia which may have a consequential impact on the Group's financial performance and relationships
- Type 26 frigate selected for the Commonwealth of Australia's Hunter Class nine-ship Future Frigate programme with the framework agreement including the A$1.9bn (£1.1bn) scope for the initial design and productionisation signed in December

Maritime

- HMS Queen Elizabeth has undergone successful initial F-35 Lightning II flight trials
- Cost growth on the Aircraft Carrier programme has resulted in a more conservative trading of contract profitability. Sea trials of HMS Prince of Wales are expected within the next year
- Type 26 selected as the design for the Canadian Surface Combatant programme
- Receipt of the full £1.6bn contract for the seventh Astute Class submarine, Agincourt, with order intake in the year of £0.7bn
- Further £1.3bn funding extension for the Dreadnought programme received
- Offshore Patrol Vessel programme quality issues have required the creation of a £47m loss provision
- Management strengthened across segment to focus on programme schedule, execution and cost performance
- CTA International, BAE Systems' joint venture with Nexter, delivered 115 40mm cased-telescopic cannons
- In January 2019, entered into an agreement with Rheinmetall to create a joint UK-based military land vehicle design, manufacturing and support business, subject to regulatory clearance

Electronic Systems

- Continued production ramp-ups on F-35 Lightning II hardware, with initial funding on Low-Rate Initial Production Lot 13
- Further awards for APKWS® laser-guided rockets secured worth nearly $400m (£314m) and production capacity ramping towards 25,000 units per annum
- Continued growth in classified work, increasing to 11% of the business
- New facilities being established in Huntsville, Alabama and Manchester, New Hampshire to increase capacity and expand operations

- Delivered the 10,000th electric hybrid bus system and continue to pursue expanding capabilities in the air and maritime domains

Platforms & Services (US)

- Selected by the US Marine Corps for the Amphibious Combat Vehicle 1.1 programme
- One of two competitors selected for the US Army's Mobile Protected Firepower programme
- Deliveries of the first batch of M777 ultra-lightweight howitzers to the Indian Army
- Continued to deliver Mk45 Gun Systems to US and international customers
- Secured $1.3bn (£1.0bn) in new orders across the four US shipyards
- In commercial shipbuilding, activities continue to complete the final ship
- Divested the Mobile, Alabama shipbuilding yard
- Management changes made and investment in process and automation improvements being implemented to position the business for its upcoming growth phase
- An accident in a nitrocellulose drying facility at Radford sadly resulted in one fatality and injuries to two employees

Cyber & Intelligence

- New awards valued at approximately $320m (£251m) to provide motion-imagery analysis, training and research support services to the US intelligence community
- Secured a five-year, $90m (£71m) US Navy contract to provide engineering and technical support for fixed, airborne and mobile intelligence collection platforms
- Awarded additional change proposals worth $55m (£43m) to support the US Air Force ICBM Integration Support Contractor programme
- Applied Intelligence 2017 restructuring programme completed, returning the business to break-even

Guidance for 2019

Whilst the Group is subject to geopolitical uncertainties, the following guidance is provided on current expected operational performance.

Group guidance

For the year ending 31 December 2019, the Group's underlying earnings per share is expected to grow by mid-single digit compared to the full-year underlying earnings per share in 2018 of 42.9p, assuming a US$1.30 to sterling exchange rate.

The guidance is based on the measures used to monitor the underlying financial performance of the Group. Reconciliations from these measures to the financial performance measures defined in International Financial Reporting Standards for 2018 are provided on pages 12 to 16.

Segmental guidance

Electronic Systems:

– Sales, in US dollar terms, are expected to show mid-single digit growth driven by a number of electronic warfare contracts and APKWS® volumes. Some 70% of projected sales are in the 2018 closing order backlog, similar to the prior year.

– Margin[1] is expected to remain in a range of 14% to 16%.

Cyber & Intelligence comprising the US Intelligence & Security sector and Applied Intelligence:

– In aggregate, sales, in US dollar terms, are expected to be relatively stable. The US business, which represented some 70% of this segment in 2018, is expected to be largely unchanged.

– In the Applied Intelligence business some top line growth is expected, coming from both the Government and Financial Services areas.

– Margin[1] in 2019 is expected to improve to be around 7%. The US business is expected to contribute around the 8% to 9% mark. In Applied Intelligence, the business is expected to move back into profitability, albeit at an initial low margin.

Platforms & Services (US):

– Sales growth, in US dollar terms, is expected to be mid- to high single digit with increasing volumes from the US Combat Vehicles and Weapon Systems businesses, as well as higher ship repair activity. More than 80% of guidance is within the closing order backlog, a stronger starting point than at this time last year.

– Margin[1] is expected to improve to the 8% to 9% range, after the charges taken in 2018.

Air:

– Sales are expected to be some 10% higher, for activity on the new Qatar Typhoon and Hawk programme and the continued ramp-up on F-35. More than 85% of guidance is within the closing order backlog.

– Margin[1] is expected to be lower than 2018, towards the bottom end of the 11% to 13% range. There will be minimal profit recognition on the Qatar sales, given the early stage of the programme, and company-funded research and development expenditure increases for the Tempest future combat air programme.

Maritime:

– Sales are expected to be stable. Activity levels on the Carrier programme will decline as it moves towards completion. This is expected to be largely offset by increases on the Dreadnought submarine and Type 26 programmes. Around 95% of guidance is already covered by the order backlog.

– Following the charges taken on the Offshore Patrol Vessels programme in 2018, margin[1] levels are expected to improve back into the 8% to 9% range.

HQ:

– HQ costs are expected to be slightly higher than 2018.

– Underlying finance costs are expected to be slightly lower with six months of benefit from the maturing $1bn (£0.8bn) bond which carries a 6.3% coupon.

1. Underlying EBITA as a percentage of sales.

- The underlying effective tax rate is expected to increase from 18% to around 20%, with the final rate dependent on the geographical mix of profits.
- The expected increase in In-Kingdom ownership and workshare into the Group's Saudi companies will lead to an increase in the non-controlling interest expense to the Group.
- The adoption of IFRS 16 Leases is expected to increase both EBITA and finance costs by an estimated £50m, but is expected to have no material impact on earnings per share.
- The Group has delivered £2bn of free cash flow in the period 1 January 2017 to 31 December 2018, and is targeting in excess of £3bn of free cash flow over the three-year period 2019 to 2021[1]. Free cash flow generation will, however, not be linear over the three-year period and, in 2019, the cash profile of the Typhoon Qatar contract and capital expenditure required to support the growing US businesses will mean that the Group's net debt at 31 December 2019 is expected to increase slightly from the net debt at 31 December 2018.

For further information please contact:

Investors
Martin Cooper,
Investor Relations Director

Telephone: +44 (0) 3300 488830
+44 (0) 1252 383455

Email: **investors@baesystems.com**

Media Relations
Rachael Gordon,
Deputy Director, Media Relations

Telephone: +44 (0) 7793 423682

Email: **rachael.gordon@baesystems.com**

Analyst and investor presentation

A presentation, for analysts and investors, of the Group's Results for 2018 will be available via webcast at 9.00am today (21 February 2019).

Details can be found on **investors.baesystems.com**, together with presentation slides and a pdf copy of this report. A recording of the webcast will be available for replay later in the day.

About BAE Systems

At BAE Systems, our advanced defence technology protects people and national security, and keeps critical information and infrastructure secure. We search for new ways to provide our customers with a competitive edge across the air, maritime, land and cyber domains. We employ a skilled workforce of 85,800 people[2] in more than 40 countries, and work closely with local partners to support economic development by transferring knowledge, skills and technology.

1. Assuming a US$1.30 to sterling exchange rate.
2. Including share of equity accounted investments.

Preliminary results statement

Introduction

2018 was both a year of geopolitical turbulence and a transition year in terms of earnings for the Group. Production on a number of programmes began ramping up especially in the Electronic Systems, US Combat Vehicles and Submarines businesses whilst Typhoon and Hawk production stepped down, and the Aircraft Carrier build programme moved towards build completion. The order backlog grew by 25% to a record high. Key business wins were secured globally: for example on the Amphibious Combat Vehicle for the US Marine Corps, in Australia for the design and build of nine ships for the Future Frigate programme, in Qatar for the provision of 24 Typhoon and nine Hawk aircraft, and in Canada where the Type 26 design was selected for the Canadian Surface Combatant programme. These wins further strengthened the outlook and the geographic base of the Group.

Governments in the Group's key markets continue to prioritise defence and security, and there is a growing demand for the Group's capabilities, products and services. BAE Systems is a diverse and resilient company, pursuing the right strategy for long-term performance. The business has a strong order backlog giving multi-year visibility, a broad portfolio with long-term positions on key programmes with strong customer relationships and a track record of successful partnerships in international markets to develop local industry, employment and skills.

The Middle East remains unstable. In the Gulf region the Group works primarily with Oman, Qatar, Kuwait and the Kingdom of Saudi Arabia, respecting the importance of the defence and security relationships, and the strength and depth of the Group's economic ties.

To that end, agreement was reached at the end of the year with the Kingdom for BAE Systems to extend the provision of Typhoon support services.

It should be recognised, however, that the Company is reliant on the approval of export licences by a number of governments in order to continue supplies to Saudi Arabia. In this context, the position on export licensing currently adopted by the German government may affect the Group's ability to provide the required capability to the Kingdom. BAE Systems is therefore working closely with the UK government to minimise the risk of any such occurrence and the impact it would have on financial performance, the supply chain and relationships.

Within the core strategy, execution on the key strategic objectives of operational excellence, competitiveness and technological innovation is vital for the successful delivery of the order backlog to deliver future growth and in evolving the business to become a stronger, smarter and sharper organisation.

Operational excellence

Raising the bar operationally to improve delivery of the record defence order book remains the priority for the Group, in order to drive growth, strengthen customer relationships and win new and repeat work in the future. Whilst areas of the business are performing strongly and the restructuring actions taken to return the Applied Intelligence business to profitability are gaining traction, there were some disappointments on certain long-standing programmes in the Maritime and Platforms & Services (US) businesses. Steps have been taken to address these operational issues. In Maritime, Andrew Wolstenholme was appointed to lead that business with a clear focus on programme schedule and cost performance. In Platforms & Services (US), the new leadership team is maintaining a keen focus on programme execution as investments are made in operational processes and automation to meet the ramp-to-rate challenges in US Combat Vehicles and position the business for successful programme delivery during its upcoming growth phase.

Competitiveness

The Group continues to take the necessary steps to be competitive. BAE Systems' customers demand value for money and it is important that the business can demonstrate exactly that. The new organisational structure announced in 2017 became effective in 2018. Within procurement, global and national category managers are now in place and efficiencies are being delivered through supply chain rationalisation and enhanced data analytics. Increasing collaboration across the Group, industry partners and academia is becoming more important in delivering competitive offerings. The Group structure and functional councils are in place to ensure this remains a key focus area and the business will be relentless in its pursuit of competitiveness and efficiency.

Technological innovation

BAE Systems has a long heritage of developing and integrating cutting-edge technologies to create complex systems that give its customers a capability advantage. The accelerating pace of technological change is a disruptive force and a key driver of competitive advantage and, increasingly, a determinant for the Group's customers in awarding new business. Coordinated through the Chief Technology Officer, the Group is aiming to increase self-funded research and development spend over time, as well as working with customers in developing technologies for use today and into the future. In 2018, technology plans were established that supported the sector strategies. The increase in spend will be achieved through a blend of self- and jointly-funded customer programmes, and through a pipeline of investment opportunities and targeted bolt-on acquisitions.

2018 performance

US

On 28 September, the fiscal year 2019 Defense Appropriations bill was enacted. This is the first time since 2008 that the Department of Defense had funding in place by the 1 October start of the fiscal year, and provided near-term clarity for the industry and demonstrated strong bi-partisan support for defence funding under the two-year agreement passed in early 2018.

The enacted Defense Appropriations bill maintains support for the business' medium-term planning assumptions and positive momentum for military readiness and modernisation programmes. The Group's US-based portfolio remains well aligned with customer priorities and growth areas with support for many key BAE Systems programmes, including combat vehicles, F-35 Lightning II, electronic warfare programmes, and current and future precision-weapons systems.

The Group's US electronics business delivered a stand-out operational performance in 2018 especially in its core franchise positions in the high-technology areas of electronic warfare, precision-guided munitions, intelligence, surveillance and reconnaissance, and electro-optics. The business closed with a record order backlog with the portfolio well aligned with the US National Defense Strategy. The business continues to leverage these defence electronics capabilities for international programmes.

Platforms and Services (US) worked to address a number of operational challenges in the year, preparing for significant production rate increases in the US Combat Vehicles business. To help position the business to deliver during its upcoming growth phase, management changes have been made and process and automation improvements are being implemented.

Growth in the US-based Combat Vehicles business is underpinned by the ramp-up of production on the Armored Multi-Purpose Vehicle, M109A7 self-propelled howitzer and Bradley upgrade programmes, and the growth outlook was advanced in 2018 with the competitive win on the Amphibious Combat Vehicle 1.1 programme and the business' selection as one of two companies to proceed to the engineering and manufacturing development phase of the Mobile Protected Firepower programme.

Across its US shipyards, Platforms and Services (US) continues to be a leading supplier of ship repair and modernisation services to the US Navy. The ship repair and naval gun franchises are well supported by the growth outlook in US Navy budget funding.

In the US-based Intelligence & Security business, whilst market conditions remain highly competitive, the business is maintaining a high level of bid activity, and secured a number of successful wins on recompeted contracts and new business awards in mission-critical areas. The business is delivering on contracts with good programme and financial performance in the period.

An accident on 11 June in a nitrocellulose drying facility in Radford sadly resulted in one fatality and injuries to two employees. The health and safety of the Group's employees has always been and continues to be BAE Systems' highest priority.

UK

Defence and security remain a priority for the UK government. This was reaffirmed in the Modernising Defence Programme and budget updates in the year. In July, the UK government launched its Combat

Air Strategy, a significant milestone for the Group's Air sector which sends a strong signal of intent about the UK's commitment to retaining a leading position in Combat Air. The strategy will enable long-term planning in a key strategic part of the business as UK government and industry jointly invest in cutting-edge, next-generation combat air systems.

During 2018 focus remained on execution of the Group's long-term contracted positions in Air and Maritime.

In Air, the production ramp-up of rear fuselage assemblies for the F-35 Lightning II aircraft is progressing, and the business is on track to achieve full rate production in 2020. The first nine UK F-35 Lightning II aircraft arrived at RAF Marham during the year and initial operational services were stood up. As the UK and global fleets grow, securing a long-term support position on F-35 Lightning II remains a key focus for the Air business.

Following delivery of the final four Typhoon aircraft to the Royal Air Force of Oman, Typhoon production is now focused on the remaining partner nations' deliveries, sub-assembly build on the Kuwait programme and the commencement of the Qatar programme, which sustains production into the next decade. Whilst a degree of geopolitical turbulence exists, the potential pipeline for Typhoon remains positive, with opportunities both with partner nations and through exports. Securing any additional orders would further extend production. Typhoon support continues to be a high-performing line of business for the Group and the Royal Air Force has declared Typhoon meets the Centurion standard, enabling the transition of capabilities from Tornado to Typhoon as the UK Tornado fleet comes out of service in 2019.

In Maritime, there remains pressure on the Navy's near-term budgets. The Offshore Patrol Vessels programme was impacted in the year by quality issues which led to a provision being taken. Lessons learned are being applied to the other ships in build. The programme is due to complete in 2020. The Type 26 programme is on track for the first of class contractual date in the mid-2020s. Initial flight trials on HMS Queen Elizabeth off the coast of the US were completed successfully and HMS Prince of Wales is due to commence sea trials in the next year.

The strengthened management team in Barrow is delivering improved performance on both the Astute and Dreadnought submarine programmes. The major site development work at Barrow continues, and in November the new Submarines Academy for Skills and Knowledge was opened.

In January 2019, BAE Systems entered into an agreement with Rheinmetall to create a joint UK-based military land vehicle design, manufacturing and support business subject to regulatory approvals. Joining forces with Rheinmetall will bring the strength of both businesses together to be more competitive in the UK and international markets whilst maintaining many jobs in the UK. Rheinmetall will purchase a 55% stake in the existing BAE Systems UK-based combat vehicles business for £28.6m, with BAE Systems retaining 45%.

The final agreement of the terms of the UK's exit from the EU after March 2019 will be important to enable companies to prepare for potential changes in the regulatory environment. There is relatively limited UK-EU trading and movement of EU nationals into and out of BAE Systems' UK businesses, and the resulting Brexit near-term impacts across the business are likely to be limited. BAE Systems will support the UK government in achieving its aim of ensuring that the UK maintains its key role in European security and defence post-Brexit, and to strengthen bilateral relationships with key partners in Europe.

International

In an uncertain global environment with complex threats, the Group's defence and security capabilities remain highly relevant. 2018 was a strong year in widening BAE Systems' international reach and there are good prospects in existing and new international markets for its products and services in air, maritime, land and cyber.

The contract between BAE Systems and the Government of the State of Qatar for the supply of 24 Typhoon and nine Hawk aircraft to the Qatar Emiri Air Force, along with a bespoke support and training package, became effective in September, and production has commenced.

In Oman, following delivery of the final Typhoons the business is delivering on a five-year availability service for Typhoon and a support package for Hawk aircraft.

In Australia, the Group submitted bids on two significant production contracts. Whilst unsuccessful in the bid for the Land 400 Phase 2 combat vehicle programme, in June, the Commonwealth of Australia selected BAE Systems as the preferred tenderer for the Hunter Class Frigate programme to deliver nine Future Frigates for the Royal Australian Navy.

The contract providing the framework for the design and build of the ships was signed in December. The build scope is to be negotiated in due course and production of the first ship is expected to commence in South Australia in the early 2020s. This Hunter Class programme is expected, over time, to double the size of the Australian business which is currently underpinned by long-term support and upgrade programmes.

Building on this success, in February 2019, the Canadian government together with Irving Shipbuilding, selected Lockheed Martin Canada, using BAE Systems' Type 26 design, as subcontractor for the Canadian Surface Combatant programme.

In Saudi Arabia, BAE Systems continues to address current and potential new requirements as part of long-standing agreements between the UK government and the Kingdom. The Memorandum of Intent signed between the Kingdom of Saudi Arabia and the UK government in March 2018, continues to progress towards reaching an Agreement for a further 48 Typhoon aircraft, support and transfer of technology and capability. This will enable BAE Systems to continue with the Industrialisation of Defence capabilities in the Kingdom of Saudi Arabia, in support of the Saudi Arabian government's National Transformation Plan and Vision 2030.

The final assembly of the Typhoon would follow on from the Hawk programme where the first In-Kingdom final-assembled Hawk aircraft is expected to be delivered to the Royal Saudi Air Force in 2019. Agreement has been reached with the Saudi Arabian government for BAE Systems to continue to provide Typhoon support services to the Royal Saudi Air Force.

The MBDA joint venture has continued to win orders in both domestic and export markets with the order backlog once again increasing, giving clear visibility of growth in the coming years. The business also continues to invest in new products and is well placed to benefit from defence spend increases in a number of European countries and from export opportunities.

Cyber security

The UK-managed Applied Intelligence business delivered a much-improved performance following restructuring actions taken in 2017 and achieved a break-even position for the year. Focused recruitment in the second half of the year positions the business for a return to growth and profitability as the market develops. The commercial market remains highly competitive; however, cyber security is an increasingly important part of government security and a core element of stewardship for commercial enterprises in a sophisticated and persistent threat environment.

Balance sheet and capital allocation

The Group's balance sheet is managed conservatively, in line with its 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, invest in research and technology and other organic investment opportunities, and 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 would deliver on the Group's strategy.

Pension schemes

The Group's share of the pre-tax accounting net pension deficit reduced to £3.9bn (2017 £4.0bn).

Executive Committee changes

Reflecting the new organisation structure from the start of 2018 there were a number of changes to the Executive Committee. Members appointed as a result of the new structure were Chris Boardman as head of Air, Andrew Wolstenholme as head of Maritime and Julian Cracknell as head of Applied Intelligence. Other new appointments were Karin Hoeing as Group Human Resources Director and at the start of 2019 David Armstrong as Group Business Development Director following Alan Garwood's retirement.

Board changes

The Board has appointed two new non-executive directors, Nicole Piasecki and Stephen Pearce, both of whom will join the Board on 1 June 2019. Nicole is a former senior executive with Boeing who has a strong track record in strategic planning and international operations and relations. Stephen is Finance Director of Anglo American plc at present, and as such has the skills and experience necessary to succeed Nick Rose as Chairman of the Audit Committee from the beginning of next year.

Responsible business

BAE Systems continues to build a culture where its people are empowered to make the right decisions and know where to go to seek help or guidance.

Recruiting and retaining talented people is a key priority. BAE Systems wants every employee to reach their full potential within a diverse and inclusive work environment. The Group has programmes in place across the business to support strategic workforce planning, career development and retention, as well as to improve diversity and inclusion.

Summary

The business benefits from a large order backlog, with established positions on long-term programmes in the US, UK, Saudi Arabia and Australia along with a growing presence in other international markets. The Group's strategy is working, it is clear and well defined. With governments in the Group's major markets continuing to prioritise defence and security there is a strong demand for its capabilities. Through improved programme execution and maintaining the strategy and capital allocation policy, BAE Systems is well placed to maximise opportunities, manage the challenges and continue to generate good shareholder returns.

Dividends

The Board has recommended a final dividend of 13.2p for a total of 22.2p for the full year. Subject to shareholder approval at the May 2019 Annual General Meeting, the dividend will be paid on 3 June 2019 to holders of ordinary shares registered on 23 April 2019.

Glossary

We monitor the underlying financial performance of the Group using alternative performance measures. These measures are not defined in International Financial Reporting Standards (IFRS) and, therefore, are considered to be non-GAAP (Generally Accepted Accounting Principles) measures. Accordingly, the relevant IFRS measures are also presented where appropriate.

	Definition	Purpose
Financial performance measures as defined by the Group		
Sales	Revenue plus the Group's share of revenue of equity accounted investments.	Allows management to monitor the sales performance of subsidiaries and equity accounted investments.
Underlying EBITA	Operating profit excluding amortisation and impairment of intangible assets, finance costs and taxation expense of equity accounted investments (EBITA), and non-recurring items*.	Provides a measure of operating profitability that is comparable over time.
Underlying earnings per share	Basic earnings per share excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, and non-recurring items*.	Provides a measure of underlying performance that is comparable over time.
Operating business cash flow	Net cash flow from operating activities excluding taxation and including net capital expenditure, financial investment and dividends from equity accounted investments.	Allows management to monitor the operational cash generation of the Group.
Net debt	Cash and cash equivalents, less loans and overdrafts (including debt-related derivative financial instruments).	Allows management to monitor the indebtedness of the Group.
Order intake	Funded orders received from customers including the Group's share of order intake of equity accounted investments.	Allows management to monitor the order intake of subsidiaries and equity accounted investments.
Order backlog	Funded and unfunded unexecuted customer orders including the Group's share of order backlog of equity accounted investments. Unfunded orders include the elements of US multi-year contracts for which funding has not been authorised by the customer.	Supports future years' sales performance of subsidiaries and equity accounted investments.
Financial performance measures defined in IFRS		
Revenue	Income derived from the provision of goods and services by the Company and its subsidiary undertakings.	N/a
Operating profit	Profit for the year before finance costs and taxation expense. This measure includes finance costs and taxation expense of equity accounted investments.	N/a
Basic earnings per share	Basic earnings per share in accordance with International Accounting Standard 33, Earnings per Share.	N/a
Net cash flow from operating activities	Net cash flow from operating activities in accordance with International Accounting Standard 7, Statement of Cash Flows.	N/a
Other financial measures		
Net pension deficit	Net International Accounting Standard 19, Employee Benefits, deficit excluding amounts allocated to equity accounted investments.	N/a
Dividend per share	Interim dividend paid and final dividend proposed per share.	N/a

* Non-recurring items are items of financial performance which have been determined by management as being material by their size or incidence and not relevant to an understanding of the Group's underlying business performance. The Group's definition of non-recurring items includes profit or loss on business transactions, and costs incurred which are one-off in nature, for example non-routine costs or income relating to post-retirement benefit schemes, and other exceptional items which management has determined as not being relevant to an understanding of the Group's underlying business performance.

Income statement

	2018 £m	2017 (restated[1]) £m
Financial performance measures as defined by the Group[2]		
Sales	**18,407**	18,487
Underlying EBITA	**1,928**	1,974
Return on sales	**10.5%**	10.7%
Financial performance measures defined in IFRS[3]	**£m**	£m
Revenue	**16,821**	17,224
Operating profit	**1,605**	1,419
Return on revenue	**9.5%**	8.2%
Reconciliation of sales to revenue	**£m**	£m
Sales	**18,407**	18,487
Deduct Share of sales by equity accounted investments	**(2,812)**	(2,534)
Add Sales to equity accounted investments	**1,226**	1,271
Revenue	**16,821**	17,224
Reconciliation of underlying EBITA to operating profit	**£m**	£m
Underlying EBITA	**1,928**	1,974
Non-recurring items	**(154)**	(13)
Amortisation of intangible assets	**(85)**	(86)
Impairment of intangible assets	**(33)**	(384)
Financial expense of equity accounted investments	**(13)**	(34)
Taxation expense of equity accounted investments	**(38)**	(38)
Operating profit	**1,605**	1,419
Net finance costs	**(381)**	(346)
Taxation expense	**(191)**	(216)
Profit for the year	**1,033**	857
Underlying net interest expense	**(215)**	(245)
Net interest expense on retirement benefit obligations	**(106)**	(173)
Fair value and foreign exchange adjustments on financial instruments and investments	**(73)**	38
Net finance costs (including equity accounted investments)	**(394)**	(380)

Exchange rates

	2018	2017
Average		
£/$	**1.335**	1.289
£/€	**1.130**	1.141
£/A$	**1.786**	1.681
Year end		
£/$	**1.274**	1.353
£/€	**1.114**	1.126
£/A$	**1.809**	1.730

Sensitivity analysis	**£m**
Estimated impact on sales of a ten cent movement in the average exchange rate:	
$	**600**
€	**90**
A$	**35**

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.

Sales decreased by £0.1bn to £18.4bn (2017 £18.5bn) as the expected reduction in Typhoon production activity was largely offset by growth in the US businesses.

Underlying EBITA decreased by £46m to £1,928m (2017 £1,974m), giving a return on sales of 10.5% (2017 10.7%). There was an adverse exchange translation impact of £34m.

Revenue decreased by £0.4bn to £16.8bn (2017 £17.2bn), a 1% decline on a constant currency basis.

Operating profit increased by £186m to £1,605m (2017 £1,419m). 2017 included a £384m impairment in respect of the Applied Intelligence business, which is excluded from underlying EBITA. There was an adverse exchange translation impact of £31m.

Non-recurring items in 2018 of £154m comprises a Guaranteed Minimum Pension equalisation charge of £114m, and a loss on disposal of the Mobile, Alabama, shipyard of £40m. Non-recurring items in 2017 of £13m represented a loss on the disposal of the BAE Systems San Francisco Ship Repair business.

Amortisation of intangible assets is in line with the prior year at £85m (2017 £86m).

Impairment of intangible assets in 2018 related to Silversky customer-related intangibles in the Applied Intelligence business. In 2017 the charge represented the impairment of goodwill in Applied Intelligence reflecting the future level and timing of expected returns from the business.

Net finance costs, including equity accounted investments, were £394m (2017 £380m). The underlying interest charge, excluding pension accounting, and fair value and foreign exchange adjustments on financial instruments and investments decreased to £215m (2017 £245m). Net interest expense on the Group's pension deficit was £106m (2017 £173m). There was a charge in respect of fair value and foreign exchange adjustments of £73m (2017 £38m credit) on exchange translation of US dollar-denominated bonds.

Taxation expense, including equity accounted investments, of £229m (2017 £254m) reflects the Group's underlying effective tax rate for the year of 18% which reduced from 21% in 2017, benefitting from the reductions to federal taxes in the US.

The underlying effective tax rate for 2019 is expected to increase from 18% to around 20%, with the final rate dependent on the geographical mix of profits.

Looking beyond 2019, the effective tax rate will depend principally on whether there are any changes in tax legislation in the Group's most significant countries of operation, the geographical mix of profits and the resolution of open tax positions.

Earnings per share

	2018	2017 (restated[1])
Financial performance measures as defined by the Group[2]		
Underlying earnings	**£1,370m**	£1,338m
Underlying earnings per share	**42.9p**	42.1p
Financial performance measures defined in IFRS[3]		
Profit for the year attributable to equity shareholders	**£1,000m**	£827m
Basic earnings per share	**31.3p**	26.0p

Reconciliation of underlying EBITA to underlying earnings	**£m**	£m
Underlying EBITA	**1,928**	1,974
Underlying interest expense (including equity accounted investments)	**(215)**	(245)
	1,713	1,729
Taxation expense (at the underlying effective tax rate)	**(310)**	(361)
Non-controlling interests	**(33)**	(30)
Underlying earnings	**1,370**	1,338

Reconciliation of underlying earnings to profit for the year attributable to equity shareholders	**£m**	£m
Underlying earnings	**1,370**	1,338
Impact of US tax reform enacted in December 2017	**–**	58
Non-recurring items, post tax	**(126)**	(10)
Amortisation and impairment of intangible assets, post tax	**(97)**	(68)
Impairment of goodwill	**–**	(384)
Net interest expense on retirement benefit obligations, post tax	**(87)**	(137)
Fair value and foreign exchange adjustments on financial instruments and investments, post tax	**(60)**	30
Profit for the year attributable to equity shareholders	**1,000**	827
Non-controlling interests	**33**	30
Profit for the year	**1,033**	857

Underlying earnings per share for the year increased by 2% to 42.9p (2017 42.1p).

Basic earnings per share was 31.3p (2017 26.0p).

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.

Cash flow

	2018 £m	2017 £m
Financial performance measures as defined by the Group[1]		
Operating business cash flow	**993**	1,752
Financial performance measures defined in IFRS[2]	**£m**	£m
Net cash flow from operating activities	**1,200**	1,897
Reconciliation from operating business cash flow to net cash flow from operating activities	**£m**	£m
Operating business cash flow	**993**	1,752
Add back Net capital expenditure and financial investment	**464**	444
Deduct Dividends received from equity accounted investments	**(57)**	(72)
Deduct Taxation	**(200)**	(227)
Net cash flow from operating activities	**1,200**	1,897
Net capital expenditure and financial investment	**(464)**	(444)
Dividends received from equity accounted investments	**57**	72
Interest received	**25**	23
Acquisitions and disposals	**41**	(11)
Net cash flow from investing activities	**(341)**	(360)
Interest paid	**(203)**	(204)
Net sale/(purchase) of own shares	**1**	(1)
Equity dividends paid	**(703)**	(684)
Dividends paid to non-controlling interests	**(28)**	(8)
Cash flow from matured derivative financial instruments (excluding cash flow hedges)	**6**	(83)
Movement in cash collateral	**2**	(15)
Net cash flow from loans	**(7)**	–
Net cash flow from financing activities	**(932)**	(995)
Net (decrease)/increase in cash and cash equivalents	**(73)**	542
Add back Net cash flow from loans	**7**	–
Add back Cash classified as held for sale	**–**	2
Foreign exchange translation	**(188)**	301
Other non-cash movements	**102**	(55)
(Increase)/decrease in net debt	**(152)**	790
Opening net debt	**(752)**	(1,542)
Net debt	**(904)**	(752)

	£m	£m
Operating business cash flow	**993**	1,752
Interest paid, net of interest received	**(178)**	(181)
Taxation	**(200)**	(227)
Free cash flow (as defined by the Group)[3]	**615**	1,344

1. For alternative performance measure definitions see glossary on page 12.
2. International Financial Reporting Standards.
3. Operating business cash flow less interest paid (net) and taxation.

Operating business cash flow was £993m (2017 £1,752m), which includes cash contributions in respect of pension deficit funding, over and above service costs, for the UK and US schemes totalling £330m on a funding basis.

On the Qatar contract there was a net inflow of approximately £400m, which will be utilised in 2019. As anticipated, timing benefits of £400m seen in 2017 on the Saudi support contract and UK VAT payment both reversed in 2018. In the Platforms & Services (US) business, there has been working capital growth on utilisation of advance payments on international programmes, some late customer receipts, delivery delays to be recovered in the near term and new business ramp up.

Taxation payments decreased to £200m (2017 £227m) primarily reflecting lower payments in the US due to the reduction in the US federal tax rate.

Net capital expenditure and financial investment was £464m (2017 £444m). As planned, capital investment was made in support of the production ramp-up in the US Electronic Systems business.

Dividends received from equity accounted investments of £57m (2017 £72m) was primarily receipts from MBDA, FNSS and Advanced Electronics Company.

Interest received was £25m (2017 £23m).

The cash inflow in respect of **acquisitions and disposals** in 2018 of £41m reflects the reduction in the Group's shareholding in Overhaul Maintenance Company (£17m), cash acquired as part of the ASC Shipbuilding acquisition (£14m) and cash received on the sale of the Mobile, Alabama, shipyard (£12m), offset by purchases of equity accounted investments. The cash outflow in 2017 of £11m reflected costs incurred in respect of the disposal of BAE Systems San Francisco Ship Repair and the acquisition of IAP Research, Inc..

Interest paid was £203m (2017 £204m).

Equity dividends paid in 2018 represents the 2017 final (£415m) and 2018 interim (£288m) dividends.

Dividends paid to non-controlling interests increased to £28m (2017 £8m) reflecting a higher payment by Saudi Maintenance & Supply Chain Management Company, in which the Group has a 51% shareholding.

There was a **cash inflow from matured derivative financial instruments** of £6m (2017 £83m outflow). The prior year outflow arose from rolling hedges relating to balances within the Group's subsidiaries and equity accounted investments.

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

Net debt

	2018 £m	2017 £m
Components of net debt		
Cash and cash equivalents	**3,232**	3,271
Debt-related derivative financial instrument assets	**163**	60
Loans – non-current	**(3,514)**	(4,069)
Loans and overdrafts – current	**(785)**	(14)
Net debt	**(904)**	(752)

The Group's **net debt** at 31 December 2018 is £904m, a net increase of £152m from the position at the start of the year. In June 2019, a $1.0bn (£0.8bn) bond will become due for repayment.

Cash and cash equivalents of £3,232m (2017 £3,271m) are held primarily for the repayment of debt securities, pension deficit funding, payment of the 2018 final dividend and management of working capital.

Accounting policies

Changes in accounting policies and restatements

With effect from 1 January 2018, the Group adopted IFRS 15 Revenue from Contracts with Customers, which outlines principles for the measurement and recognition of revenue from contracts with customers. Comparative financial information has been restated accordingly. IFRS 9 Financial Instruments was also adopted from 1 January 2018; however no adjustments were required to prior years. Details of the impact of IFRS 15 and IFRS 9 are provided in note 11.

Effective 1 January 2019, BAE Systems adopted IFRS 16 Leases. The Group's results announcement for the half year ending 30 June 2019 will be the first to be prepared under IFRS 16. The Group will transition in accordance with the modified retrospective approach, and prior year information will not be restated.

IFRS 16 requires a lessee to recognise assets and liabilities for almost all leases. In the income statement, operating lease charges will be replaced by depreciation and interest expenses. The estimated impact on the Group in 2019 is expected to be an increase in EBITA of £50m, offset by an increase in finance costs of £50m, with an immaterial impact on profit after tax and underlying earnings. On transition, right-of-use assets will be recognised on the balance sheet of £1,300m with a lease liability of £1,486m and a transition adjustment of £92m will be recognised as a debit to retained earnings. The Group will also recognise a finance lease receivable balance of £70m, a reduction in the investment in equity accounted investments of £11m and a deferred tax asset of £2m. Details of the impact of IFRS 16 are provided in note 12.

Segmental review

The Group reports its performance through five principal reporting segments[1].

	Year ended 31 December 2018									
	As defined by the Group						Defined in IFRS[2]			
	Sales £m	Underlying EBITA £m	Return on sales %	Operating business cash flow £m	Order intake[3] £m	Order backlog[3] £bn	Revenue £m	Operating profit/ (loss) £m	Return on revenue %	Net cash flow from operating activities £m
Electronic Systems	3,965	606	15.3	431	4,624	5.4	3,965	590	14.9	575
Cyber & Intelligence	1,678	111	6.6	85	1,802	1.9	1,678	59	3.5	96
Platforms & Services (US)	3,005	210	7.0	(30)	3,693	5.4	2,864	161	5.6	31
Air	6,712	859	12.8	666	14,845	27.4	5,579	810	14.5	719
Maritime	2,975	209	7.0	67	3,513	9.0	2,940	191	6.5	190
HQ[4]	350	(67)		(226)	358	0.1	41	(206)		(211)
Deduct Intra-group	(278)				(555)	(0.8)	(246)			
Deduct Taxation[5]										(200)
Total	**18,407**	**1,928**	**10.5**	**993**	**28,280**	**48.4**	**16,821**	**1,605**	**9.5**	**1,200**

	Year ended 31 December 2017 (restated[6])									
	As defined by the Group						Defined in IFRS[2]			
	Sales £m	Underlying EBITA £m	Return on sales %	Operating business cash flow £m	Order intake[3] £m	Order backlog[3] £bn	Revenue £m	Operating profit/ (loss) £m	Return on revenue %	Net cash flow from operating activities £m
Electronic Systems	3,598	541	15.0	450	4,175	4.8	3,598	521	14.5	569
Cyber & Intelligence	1,818	58	3.2	116	1,859	2.1	1,818	(361)	(19.9)	127
Platforms & Services (US)	2,951	237	8.0	222	3,542	4.2	2,848	213	7.5	286
Air	7,210	967	13.4	832	6,128	19.5	6,312	918	14.5	888
Maritime	2,877	251	8.7	278	4,671	8.5	2,845	240	8.4	396
HQ[4]	336	(80)		(146)	337	–	47	(112)		(142)
Deduct Intra-group	(303)				(455)	(0.4)	(244)			
Deduct Taxation[5]										(227)
Total	18,487	1,974	10.7	1,752	20,257	38.7	17,224	1,419	8.2	1,897

1. With effect from 1 January 2018, the Group revised its reporting segments to reflect the organisational changes announced in 2017. The five principal reporting segments are Electronic Systems, Cyber & Intelligence, Platforms & Services (US), Air and Maritime. Financial information for 2017 has been re-presented to reflect these new reporting segments.
2. International Financial Reporting Standards.
3. Including share of equity accounted investments.
4. HQ comprises the Group's head office activities, together with a 49% interest in Air Astana.
5. Taxation is managed on a Group-wide basis.
6. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Segmental performance: Electronic Systems

Electronic Systems, with 15,900 employees[1], comprises the US and UK-based electronics activities, including electronic warfare systems, electro-optical sensors, military and commercial digital engine and flight controls, precision guidance and seeker solutions, next-generation military communications systems and data links, persistent surveillance capabilities, and hybrid electric drive systems.

Operational and strategic key points

- Continued production ramp-ups on F-35 Lightning II hardware, with initial funding on Low-Rate Initial Production Lot 13
- Further awards for APKWS® laser-guided rockets secured worth nearly $400m (£314m) and production capacity ramping towards 25,000 units per annum
- Continued growth in classified work, increasing to 11% of the business
- New facilities being established in Huntsville, Alabama and Manchester, New Hampshire to increase capacity and expand operations
- Delivered the 10,000th electric hybrid bus system and continue to pursue expanding capabilities in the air and maritime domains

Financial performance

Financial performance measures as defined by the Group[2]

	2018	2017 (restated[4])
Order intake[1]	**£4,624m**	£4,175m
Order backlog[1]	**£5.4bn**	£4.8bn
Sales	**£3,965m**	£3,598m
Underlying EBITA	**£606m**	£541m
Return on sales	**15.3%**	15.0%
Operating business cash flow	**£431m**	£450m

Financial performance measures defined in IFRS[3]

	2018	2017 (restated[4])
Revenue	**£3,965m**	£3,598m
Operating profit	**£590m**	£521m
Return on revenue	**14.9%**	14.5%
Cash flow from operating activities	**£575m**	£569m

- Sales compared to 2017, in US dollar terms, were up 14% at $5.3bn (£4.0bn). The growth came in the electronic warfare business from the F-35 programme as well as increasing classified activity. As expected, sales of the APKWS® product doubled over the year and now represent one of the top three sales lines in the segment. Commercial sales of engine and flight controls, and hybrid electric drive units also grew, and amount to some 22% of the segment.
- Underlying EBITA was up to $809m (£606m), delivering a return on sales of 15.3%, within our guidance range.
- As expected, cash conversion of EBITA improved in the second half of the year and was at 81% for the full year excluding pension deficit funding. Capital expenditure in the business amounted to some $200m (£150m).
- Order backlog was secured at a record high of $6.9bn (£5.4bn), following awards for further F-35 systems, classified electronic warfare activity and APKWS® units.

Operational performance

Electronic Combat

BAE Systems continues to sustain its leadership position in the US electronic warfare market with production continuing to ramp-up across a number of programmes, some of which are classified. Low-Rate Initial Production Lot 11 hardware deliveries continue on the F-35 Lightning II programme. We have received initial Lot 12 and 13 funding, and are currently negotiating Lots 12, 13 and 14 with an anticipated final award value exceeding $1bn (£0.8bn). BAE Systems is also executing an Electronic Warfare Performance Based Logistics contract from Lockheed Martin to provide material availability and support for the F-35 programme over a five-year period.

Following our 2015 selection by Boeing to develop and manufacture the next-generation digital electronic warfare system for the US Air Force's Eagle Passive Active Warning Survivability System (EPAWSS) programme to upgrade up to 200 F-15E aircraft, we are currently executing the $194m (£152m) engineering and manufacturing development contract, with a critical system delivery completed in 2018.

Under a contract by Boeing and Warner Robins Air Logistics Complex totalling more than $1bn (£0.8bn), BAE Systems completed the installation of the Digital Electronic Warfare System (DEWS) on new F-15 aircraft, and continues to upgrade existing F-15 aircraft and provide spare units and modules for an international customer. We are also executing a $311m (£244m) contract to provide DEWS to support the sale of new F-15 aircraft to another international customer.

Production of BAE Systems' sensor technology for the Long Range Anti-Ship Missile (LRASM) continues with orders from prime contractor Lockheed Martin. We provided the sensor technology that supported several successful tests of LRASM leading to a successful Early Operational Capability on the B1-B platform. We have also been awarded the LRASM Radio Frequency Sensor 110 Production Build valued at over $75m (£59m).

For over a decade, we have provided full-lifecycle support as the prime mission system integrator for the US Air Force's EC-130H Compass Call stand-off electronic attack platform, and we will continue to sustain the existing EC-130H electronics. We also execute multiple contracts to cross-deck the mission electronics onto a new Gulfstream G550 business jet for the US Air Force.

Due to the sensitive nature of electronic combat systems and technology, many of our programmes are classified. As a world leader in electronic warfare, we continue to experience growth in these increasingly important areas.

Survivability, Targeting & Sensing

Our Advanced Precision Kill Weapon System (APKWS®) laser-guided rocket is experiencing growing demand, with over 25,000 units produced as at year end. In addition to expanding US military use, the system is generating strong international attention, with 20 nations expressing formal interest. The programme has received awards totalling nearly $400m (£314m) this year, as part of a 2016 Indefinite Delivery, Indefinite Quantity contract. Production capacity is set to increase from 10,000 units per annum to 25,000 units per annum to meet the increased demand for cost-effective guided munitions for US armed forces and allied international customers.

We are developing a next-generation missile warning system for the US Army under the Limited Interim Missile Warning System programme awarded in 2017. Critical design reviews and initial prototypes have been completed on schedule.

The US Army's Family of Weapon Sights – Crew Served programme is in development testing. This seven-year contract awarded in 2016 has a potential value of up to $384m (£301m).

Both fixed and rotary-wing demonstrations of our Striker® II helmet-mounted display (HMD) are ongoing and we continue to validate it as a readily accessible HMD for existing aircraft with analogue-based or digital electronic systems.

The LiteHUD® Head-Up Display has completed development testing and has been selected by critical launch customers for integration on multiple platforms, including the Textron Scorpion jet.

C4ISR Systems

As a leading provider of space-qualified subsystems and components, we continue to experience growth in the areas of integrated on-board processors, reconfigurable processing payloads and secure communications.

We continue to execute the Network Tactical Common Data Link programme to provide the US Navy with the ability to simultaneously transmit and receive real-time intelligence, surveillance and reconnaissance data over multiple data links for a system to be fielded on various surface ship types. The programme completed Critical Design Review in 2018.

Since winning the Geospatial Data Services Foundational GEOINT Content Management programme in 2014, we have been awarded orders valued at $240m (£188m) and are meeting delivery requirements in assisting US intelligence community customers with the development of advanced geospatial intelligence data collection and processing solutions.

As a provider of signals intelligence capabilities, user acceptance under the $132m (£104m) Tactical Signals Intelligence Payloads programme for the US Army's Gray Eagle unmanned aircraft is complete. Follow-on awards are expected in 2019.

Work continues on state-of-the-art processing capabilities for the US Navy's P-8A Poseidon maritime surveillance aircraft programme which is expected to be worth $1.2bn (£0.9bn) over its life. We have delivered our hundredth system.

Controls & Avionics

BAE Systems is a major supplier of full authority digital engine controls (FADECs), fly-by-wire flight controls, vehicle management systems, mission systems, and cabin and flight deck systems.

The development of the integrated flight control electronics and remote electronic units for Boeing's next-generation 777X aircraft is progressing, with all hardware in qualification and systems integration testing to support a 2019 first flight.

Flight testing of the Boeing 737 MAX 7 aircraft is continuing with our spoiler controls, flight deck systems and utilities electronics, with entry into service planned for 2019. Initial development has begun on the changes required for the MAX 10 variant.

Development of our civil active inceptors for the Gulfstream G500 and Embraer KC390 aircraft is complete and aircraft certification has been received. A derivative of the active inceptors, the LinkEdge™ (Active Parallel Actuation Subsystem), is being developed for the Chinook CH-47 and is currently in integration testing.

FADEC Alliance, a joint venture between GE Aviation and FADEC International (our joint venture with Safran Electronics & Defense), has broadened its agreement with GE Aviation to include collaboration on system architectures and technologies for future engines. FADEC Alliance will develop, produce and support FADECs for all future GE Aviation commercial engines. The GE9X FADEC for the Boeing 777X has completed certification testing and low-rate initial production will begin in 2019.

Development has begun on the next generation advanced digital flight control computer for the F-16 aircraft for the United Arab Emirates.

On the F-35 Lightning II programme, Low-Rate Initial Production Lot 11 is ongoing for the vehicle management computer and active inceptor system equipment, and a successful systems requirements review was held on the competitively-awarded F-35 vehicle management computer technology refresh.

Power & Propulsion Solutions

This year we achieved a major milestone, delivering our 10,000th electric hybrid bus system and we continue to pursue expanding our capabilities for application in the maritime domain, and for the airborne market by marrying our safety-critical know-how from the Controls & Avionics business with our hybrid-electric expertise. As transit operators in cities such as San Francisco, Boston, Montreal, London and Brussels lean toward more electric power, our solutions meet operational goals towards totally emission-free operations. We are prepared for the future of transit with zero emission solutions as early providers of battery-electric propulsion solutions and hydrogen fuel cell-based systems. Paris has recently become the latest city to commit to battery-electric vehicles powered by our technology and in the US more than 20 hydrogen fuel cell transit buses are operating with our propulsion systems, which are expected to pave the way for the world's first passenger vessel powered by hydrogen in 2019.

We are also using our clean technology to power passenger vessels, research vessels, and inland towboats to address the increased demand for environmentally friendly marine vessels.

Looking forward

Forward-looking information for the Electronic Systems reporting segment is provided on page 38.

1. Including share of equity accounted investments.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.
4. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Segmental performance: Cyber & Intelligence

Cyber & Intelligence, with 10,300 employees[1], comprises the US-based Intelligence & Security business and UK-headquartered Applied Intelligence business, and covers the Group's cyber security, secure government, and commercial and financial security activities.

Operational and strategic key points

Intelligence & Security

- New awards valued at approximately $320m (£251m) to provide motion-imagery analysis, training and research support services to the US intelligence community
- Secured a five-year, $90m (£71m) US Navy contract to provide engineering and technical support for fixed, airborne and mobile intelligence collection platforms
- Awarded additional change proposals worth $55m (£43m) to support the US Air Force ICBM Integration Support Contractor programme

Applied Intelligence

- 2017 restructuring programme completed, returning the business to break-even

Financial performance

Financial performance measures as defined by the Group[2]

	2018	2017 (restated[4])
Order intake[1]	**£1,802m**	£1,859m
Order backlog[1]	**£1.9bn**	£2.1bn
Sales	**£1,678m**	£1,818m
Underlying EBITA	**£111m**	£58m
Return on sales	**6.6%**	3.2%
Operating business cash flow	**£85m**	£116m

Financial performance measures defined in IFRS[3]

	2018	2017 (restated[4])
Revenue	**£1,678m**	£1,818m
Operating profit/(loss)	**£59m**	£(361)m
Return on revenue	**3.5%**	(19.9)%
Cash flow from operating activities	**£96m**	£127m

- In aggregate sales were 5% lower on a constant currency basis at $2.2bn (£1.7bn). The US Intelligence & Security business saw a 4% decrease, largely as a result of the customer's decision to end a shared IT services environment contract. In the Applied Intelligence business, sales declined by 9% as pursuit of sales growth was tempered to enhance profit performance.
- Despite the sales reduction, the aggregate return on sales for the sector was improved to 6.6%. In the US business return on sales was similar to last year at 9.0%. The Applied Intelligence business returned to break even as the cost reduction actions under the 2017 restructuring programme delivered to plan.
- Cash conversion of EBITA for the year was at 95%, excluding pension deficit funding.
- In aggregate, order backlog reduced to $2.4bn (£1.9bn). In the US Intelligence & Security business, order backlog was adjusted for the closed out service contract.

Operational performance

Intelligence & Security

Air Force Solutions

We were awarded engineering change proposals valued at more than $55m (£43m) under the US Air Force Intercontinental Ballistic Missile Integration Support Contractor programme. The awards increased the total lifecycle value of the programme to $972m (£763m). Our work includes programme management, systems engineering, integration and testing, sustainment, and cyber defence.

To support US Air Force testing and training operations, we were awarded contracts totalling just over $58m (£46m) in 2018 to provide a proprietary electronic warfare/electronic attack solution.

Our business earned a position on a new nine-year Indefinite Delivery, Indefinite Quantity contract with the US Department of Defense, which positions us to bid on upcoming research, development, testing, and evaluation task orders to support the future needs of the US military across physical and digital domains. The contract affords us opportunities to leverage our investments in artificial intelligence and machine learning.

We secured a three-year, $37m (£29m) contract to continue providing the US Air Force with obsolescence management support for which we have been the provider of choice since 1991.

Integrated Defense Solutions

Our US Navy Strategic Systems Program experts are executing the third year of a five-year, $368m (£289m) sole-source contract to support weapons systems on board US Ohio and UK Vanguard Class submarines, as well as future Ohio Class replacement and UK Dreadnought Class submarines.

In October, we secured a five-year, $106m (£83m) contract to continue providing logistics and information technology support services to the US Navy's Strategic Systems Program. Our team provides logistics support for the US and UK Navy's Trident II submarines, US submarine support facilities, and US Ohio Class guided-missile submarines.

In November, we earned a five-year, $79m (£62m) contract to continue maintaining and operating multiple electronic, communication, and computing platforms for the US Navy. The programme, which supports the Naval Computer and Telecommunications Area Master Station, Pacific, provides 24/7 mission support for ship-to-shore, shore-to-aircraft, and shore-to-shore long-range communications systems.

Also in the maritime domain, we received a five-year, $90m (£71m) US Navy contract to continue providing engineering and technical support for a variety of fixed, airborne, and mobile intelligence collection platforms. The business also secured a four-year, $44m (£35m) contract to provide munitions handling and management support for the US Navy's Pacific fleet.

We were selected for Indefinite Delivery, Indefinite Quantity contracts to pursue new work in support of the US government. Two of the contracts are single-award, with a total potential value of more than $150m (£118m) to support the rapid integration and sustainment of command, control, communications, reconnaissance, and combat systems for the Naval Air Warfare Center Aircraft Division. Under the third contract, which has a maximum value of $72m (£57m), we will compete for future task orders to provide equipment modification, system safety work, test bed operations, and technical services to support air traffic control and landing systems on ships and at US Navy facilities.

Intelligence Solutions

New task order contracts valued at approximately $320m (£251m) were won to provide motion-imagery analysis, training, and research support services to the US intelligence community.

The US Army awarded the business a four-year, $100m (£79m) contract to provide technical, functional, and general support to enhance the overall situational awareness and training of troops deployed around the world.

A US Department of Defense contract to continue providing mission-critical intelligence analysis support for forward-deployed soldiers was revised by the customer to a total lifecycle value of more than $110m (£86m) over an 18-month period.

We secured a five-year, $73m (£57m) contract to expand our analysis portfolio in support of the US intelligence community.

Applied Intelligence

Applied Intelligence delivered a full year break-even position as a result of significant benefits from the restructuring activity undertaken at the end of 2017. This improvement in profitability has been delivered through removing surplus delivery capacity, relocating roles to lower cost international delivery centres, exiting certain unprofitable markets and improving the organisational structure. Following the embedding of the organisational changes, the second half of the year has seen an increase in headcount and focused investment initiatives to drive higher levels of growth in the future.

Government

The Government business has delivered growth in orders from key accounts across UK government customers as demand for our national security and intelligence offerings remains strong. There has been an increased focus on investment in our people throughout the year to enhance capability required to support specialist customer requirements while also improving employee retention in a competitive labour market.

Financial Services

The business has continued to see steady demand for anti-fraud and regulatory compliance products across multi-national financial institutions. Strong customer loyalty has been maintained through a number of product upgrades with established key accounts. Investment in product engineering, primarily NetReveal® and Managed Security Services, has increased in the year to drive higher levels of demand in 2019 and beyond. Emerging product offerings, such as broader data and digital services, are also proving to be in demand.

Technology & Commercial

The business has won a number of significant multi-year Managed Security Services deals with UK and US commercial customers in the year, facilitated by investment in the product offering to enhance customer experience. We continue to see high levels of demand for the outsourcing of security monitoring through specialist operations centres, driven in the main by the increasing importance companies are placing on mitigating ever-increasing cyber risks. The level of customer churn with US small and medium-sized businesses has increased in the year, contributing to reduced revenue levels in this area.

Looking forward

Forward-looking information for the Cyber & Intelligence reporting segment is provided on page 38.

1. Including share of equity accounted investments.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.
4. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Segmental performance: Platforms & Services (US)

Platforms & Services (US), with 11,900 employees[1], has operations in the US, UK and Sweden. It manufactures combat vehicles, weapons and munitions, and delivers services and sustainment activities, including ship repair and the management and operation of government-owned munitions facilities.

Operational and strategic key points

– Selected by the US Marine Corps for the Amphibious Combat Vehicle 1.1 programme
– One of two competitors selected for the US Army's Mobile Protected Firepower programme
– Deliveries of the first batch of M777 ultra-lightweight howitzers to the Indian Army
– Continued to deliver Mk45 Gun Systems to US and international customers
– Secured $1.3bn (£1.0bn) in new orders across our four US shipyards
– In commercial shipbuilding, activities continue to complete the final ship
– Divested the Mobile, Alabama shipbuilding yard
– Management changes made and investment in process and automation improvements being implemented to position the business for its upcoming growth phase
– An accident in a nitrocellulose drying facility at Radford sadly resulted in one fatality and injuries to two employees

Financial performance

Financial performance measures as defined by the Group[2]

	2018	2017 (restated[4])
Order intake[1]	**£3,693m**	£3,542m
Order backlog[1]	**£5.4bn**	£4.2bn
Sales	**£3,005m**	£2,951m
Underlying EBITA	**£210m**	£237m
Return on sales	**7.0%**	8.0%
Operating business cash flow	**£(30)m**	£222m

Financial performance measures defined in IFRS[3]

	2018	2017 (restated[4])
Revenue	**£2,864m**	£2,848m
Operating profit	**£161m**	£213m
Return on revenue	**5.6%**	7.5%
Cash flow from operating activities	**£31m**	£286m

– Sales, in US dollar terms, in the year were up 5% to $4.0bn (£3.0bn) but growth was behind guidance, due to the delayed Paladin production order award, and the Ship Repair customer requirement to award each ship individually, rather than multi-ship awards, meant we have not been able to maximise shipyard utilisation.
– Return on sales for the year was at 7.0% following the charges taken in the first half of the year on the remaining commercial shipbuilding contract and for the subcontractor performance issues on the Radford facilities construction programme. There were no further charges taken on those programmes in the second half of the year. The charges impacted return on sales by 150bps.
– Cash flow performance in the year reflects advance payment utilisation on international programmes, some late customer receipts, delivery delays to be recovered in the near term, and new business ramp-up.
– Order backlog increased to $6.8bn (£5.4bn), supportive of future growth expectations. Key awards in the year included Low-Rate Initial Production for the Amphibious Combat Vehicle for the US Marine Corp, Armored Multi-Purpose Vehicle, Low-Rate Initial Production on Paladin and the Mobile Protected Firepower engineering and manufacturing development phase for the US Army, as well as growth in Ship Repair.

Operational performance

US Combat Vehicles

The business continues to address manufacturing and execution challenges on some programmes as it ramps-up production levels. Measures undertaken in the period include management changes and investments in modernising facilities and manufacturing technologies, to include automation and robotic welding.

In June, BAE Systems and industry teammate Iveco Defence Vehicles were selected to supply Amphibious Combat Vehicles (ACV) for the US Marine Corps under the competitively-awarded ACV 1.1 programme phase. Low-Rate Initial Production has begun under a contract initially valued at $198m (£155m) for 30 vehicles, with options for a total of 204 vehicles worth up to $1.2bn (£0.9bn). A second, $140m (£110m) contract for Low-Rate Initial Production 2 for an additional 30 vehicles was awarded in December.

In December, the US Army awarded us a $376m (£295m) contract under the Mobile Protected Firepower programme for the engineering and manufacturing development phase for rapid prototyping efforts and with Low-Rate Initial Production options included. We were one of two competitors selected for this phase. The Army is expected to down select to a single contractor for the Low-Rate Initial Production phase in the first half of 2022.

On the US Army's Armored Multi-Purpose Vehicle programme, in August we received a $298m (£234m) contract to procure long-lead material to support Low-Rate Initial Production. The original 2014 contract included the engineering and manufacturing development and Low-Rate Initial Production phases with a potential cumulative value of $1.2bn (£0.9bn). In 2019, we have been awarded contract modifications worth up to $575m (£451m) for Low-Rate Initial Production options.

Work continues on a $365m (£287m) contract for the fourth Low-Rate Initial Production phase for 48 Paladin self-propelled howitzer and ammunition carrier vehicles sets, with an option for an additional 12. A full-rate production decision is expected in 2019.

The business is nearing completion on a $322m (£253m) engineering and manufacturing development contract to address the space, weight, power and cooling limitations of the Bradley family of vehicles and to prepare the vehicle for communication network upgrades. In June we received a $348m (£273m) contract, initially funded at $132m (£104m), to upgrade 164 vehicles to the Bradley A4 configuration.

We continue to work on US Army contracts awarded in 2017 for upgrades and sustainment of M88 recovery vehicles, to include upgrades to the Heavy Equipment Recovery Combat Utility Lift Evacuation Systems (HERCULES) configuration. In July, we received a $114m (£90m) contract for the follow-on production.

Internationally, we completed deliveries in 2018 of 41 Assault Amphibious Vehicles (AAVs) to Japan under contracts totalling $165m (£130m). We continue to work on an additional 11 vehicles for Japan. All of the 23 AAVs ordered by Brazil under an $82m (£64m) contract were also delivered, and work has begun on an $84m (£66m) contract with Taiwan for 36 AAVs.

We continue to execute a $54m (£42m) contract to provide 32 upgraded self-propelled howitzers to the Brazilian Army, with first deliveries to take place in 2019.

Weapon Systems

We have delivered the first M777 ultra-lightweight howitzers to the Indian Army under a $542m (£426m) Foreign Military Sale contract to provide 145 M777s. We are building the first 25 guns in our facilities, with the remaining systems assembled in India by Mahindra Defence Systems, our selected supplier, who has established an assembly and integration facility in India.

We are executing on a $47m (£37m) contract modification from the US Navy in December 2017 to deliver four additional Mk45 Gun Systems upgraded to increase firepower and extend range. We also received contracts to provide additional 57mm Mk110 gun systems for the Navy's Littoral Combat Ship programme, and the US Coast Guard's National Security Cutter Legend Class and Offshore Patrol Cutter programmes.

In March, we received a contract to provide eight payload tubes for two block V version Virginia Class submarines, each featuring a new payload module for increased firepower.

Work continues under a 2017 contract to deliver 155mm BONUS ammunition to the Swedish Army, and we were awarded a further contract in 2018 for delivery of the round to the US Army. The business is delivering 24 additional Archer artillery systems under a 2016 contract modification with the Swedish government. In December, we received a contract from the Swedish Armed Forces for two of the newest 40 Mk4 gun systems.

We continue to execute on a $183m (£144m) contract to provide the Maritime Indirect Fire System for the Royal Navy's Type 26 frigate.

We achieved a fifth consecutive award term providing world-wide lifecycle support for the M777 ultra-lightweight howitzers that are in service with the US Marine Corps and Army. This support contract includes engineering maintenance, parts repair/replacement and other field- and depot-level service support. The M777 team, from both the US and UK, has now scored five consecutive 'excellent' ratings, a 100% record, resulting in the contract's extension until May 2023.

In the complex ordnance manufacturing business, we continue to manage and operate the US Army's Radford and Holston munitions facilities under previously-awarded contracts. In September, the Army awarded a $97m (£76m) contract modification for the construction of a natural gas-fired steam facility at Holston. Also at Holston, we are progressing on modernisation contracts totalling $135m (£106m) for waste water management and a $146m (£115m) contract for the construction of a nitric acid recovery facility to produce larger quantities of insensitive munitions. At Radford, subcontractor performance issues and cost overruns on the nitrocellulose facility modernisation programme have been encountered, impacting the financial performance of the sector.

We are saddened to report that an accident on 11 June in a nitrocellulose drying facility in Radford resulted in one fatality and injuries to two employees. The health and safety of our employees has always been and continues to be our highest priority. Investigations concluded the accident likely resulted from a unique set of conditions, and processes were modified to prevent future occurrences.

US Ship Repair

As a leading provider of US Navy ship repair and modernisation services, we are strategically located in four of the US Navy's primary ports, with the homeported fleet projected to grow in San Diego and Jacksonville. Our shipyards are equipped to service a broad range of maritime vessels, to include cruisers, destroyers, amphibious warships and littoral combat ships for the US Navy, as well as select private and commercial vessels.

In 2018, we secured firm orders across our US shipyards totalling approximately $1.3bn (£1.0bn), including awards to modernise the USS Philippine Sea in Jacksonville; the USS Gettysburg in Norfolk; and the USS Sterett in San Diego.

In commercial shipbuilding, completion, outfitting and delivery activities for the final ship, Hull 113, continued. Hull 112 remains a completed asset held on our balance sheet awaiting the identification of a new buyer and final sea trials.

Earlier in 2018, we ceased operations at our Mobile shipyard and in October, we completed the divestiture of the shipyard.

BAE Systems Hägglunds

With an installed base of nearly 1,300 CV90 vehicles in Sweden and across six other international markets, the business continues to execute and pursue a number of significant CV90 contracts.

We continue to evaluate the opportunity for the CV90 into Australia's LAND 400 Phase 3 competition for a Mounted Close Combat Capability family of vehicles. Our bid with teammate Patria for the LAND 400 Phase 2 Combat Reconnaissance Vehicle was unsuccessful.

We continue to advance local industrial cooperation arrangements with Czech companies in support of an anticipated bid of the CV90 for the country's next fleet of infantry fighting vehicles.

Work continues to refurbish Swedish CV90 vehicles under a contract awarded in 2016, and we are integrating Mjölner mortar systems on 40 Swedish CV90s under a separate contract.

Initial deliveries have begun under a contract for 32 BvS10 all-terrain vehicles for Austria. We are also pursuing opportunities for the BvS10 and its unarmoured sister Beowulf vehicle in the US.

FNSS

FNSS, our land systems joint venture based in Turkey, continues to perform under its $524m (£411m) programme to produce 259 8x8 wheeled armoured vehicles for the Royal Malaysian Army.

Programme deliveries are on schedule under the contract with Oman for PARS Wheeled Armoured Vehicles in 8x8 and 6x6 configurations.

Work progresses under multiple contracts to Turkish Armed Forces, including a €278m (£250m) contract to supply 260 Anti-Tank Vehicles, an €84m (£75m) contract for air defence vehicles, and a €155m (£139m) contract to provide 27 amphibious assault vehicles.

Looking forward

Forward-looking information for the Platforms & Services (US) reporting segment is provided on page 38.

1. Including share of equity accounted investments.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.
4. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Segmental performance: Air

Air, with 27,800 employees[1], comprises the Group's UK-based air activities for European and International markets, and US Programmes, and its businesses in Saudi Arabia and Australia, together with its 37.5% interest in the European MBDA joint venture.

Operational and strategic key points

- Contract with the Qatar government for the supply of 24 Typhoon and nine Hawk aircraft, air and ground training, and ground support became effective in September. MBDA contract for the supply of missiles also became effective
- Signature in March 2018 of a Memorandum of Intent between the Kingdom of Saudi Arabia and the UK government to aim to finalise discussions for the purchase of a further 48 Typhoon aircraft
- RAF declaration of Typhoon Centurion standard, enabling transition of capabilities from Tornado to Typhoon
- Announcement of the UK Combat Air Strategy and launch of the Tempest programme
- Completion of the final four of 12 Typhoon deliveries to Oman
- In November the first flight of a Hawk assembled in Saudi Arabia took place
- Integration of F-35 Lightning II onto aircraft carrier HMS Queen Elizabeth commenced, and the first F-35 deck landing completed
- Order intake of £3.2bn for support services up to 2022 in respect of the continuation of Typhoon support in Saudi Arabia
- Current German government position on export licensing may affect the Group's ability to provide capability to Saudi Arabia which may have a consequential impact on the Group's financial performance and relationships
- Type 26 frigate selected for the Commonwealth of Australia's Hunter Class nine-ship Future Frigate programme with the framework agreement including the A$1.9bn (£1.1bn) scope for the initial design and productionisation signed in December

Financial performance

Financial performance measures as defined by the Group[2]

	2018	2017 (restated[4])
Order intake[1]	**£14,845m**	£6,128m
Order backlog[1]	**£27.4bn**	£19.5bn
Sales	**£6,712m**	£7,210m
Underlying EBITA	**£859m**	£967m
Return on sales	**12.8%**	13.4%
Operating business cash flow	**£666m**	£832m

Financial performance measures defined in IFRS[3]

	2018	2017 (restated[4])
Revenue	**£5,579m**	£6,312m
Operating profit	**£810m**	£918m
Return on revenue	**14.5%**	14.5%
Cash flow from operating activities	**£719m**	£888m

- Sales were down 7% at £6.7bn. As expected production activity on Typhoon for the European, Saudi and Oman contracts has largely completed. The F-35 programme continues to ramp-up to plan and Middle East support volumes continue to grow.
- The return on sales of 12.8% was at the top end of our guidance. There has been some profit trading on completing the Typhoon Oman contract with minimal sales and that has generated a 70bps benefit within the reported return on sales.
- The £666m of cash inflow in the year reflects full consumption of the £300m early receipts seen in 2017 against the Saudi Arabia support programme, utilisation of advances on the residual Typhoon export contracts, and a net advance now held on the Qatar programme.
- Order backlog stands at £27.4bn, significantly higher following the awards for the £5.1bn Qatar Typhoon and Hawk programme, the £1.1bn initial contract under the Australian Hunter Class frigate programme, and £3.2bn for the continuation of support services for Typhoon in Saudi Arabia.

Operational performance

European & International markets

The contract entered into between BAE Systems and the Government of Qatar, valued at approximately £5bn, for the supply of 24 Typhoon and nine Hawk aircraft became effective during September. The agreement also provides for the supply of ground support and training to the Qatar Armed Forces. The business has begun mobilising resources and supply chain.

The final four out of a total of 12 Typhoon aircraft were delivered to the Royal Air Force of Oman during the year. The five-year availability service contract for the aircraft continues.

Production is ongoing under the Kuwait Typhoon contract, secured by Italian Eurofighter partner Leonardo, with all 28 major units now in work. BAE Systems deliveries will commence in 2019.

In the year, the Royal Air Force accepted seven Typhoon aircraft from the UK final assembly facility. The German, Italian and Spanish Air Forces accepted a total of 15 aircraft, which brings deliveries of Tranche 3 aircraft to 73 of the 88 contracted.

The Royal Air Force declared Typhoon to have met Centurion standard, enabling the transition of capabilities from Tornado to Typhoon. Integration of the Captor E-Scan radar continues to progress as we conduct first flight trials to develop and improve the radar's capability.

In the UK we continue to support the Ministry of Defence Typhoon fleet under a ten-year partnership arrangement which provides flying hours and we also support the European Partner Nations support arrangements at above contractual levels.

Following the £119m contract secured in 2017 for collaboration on the first design and development phase of an indigenous fifth-generation fighter jet for the Turkish Air Force, activity has focused on mobilising resources.

Discussions with the Government of India and Hindustan Aeronautics Limited (HAL) for the supply of Hawk aircraft kit sets to be used to build additional aircraft under licence in India for the Indian Air Force and Navy, have ceased pending a clearer understanding of their requirements.

Support to the Royal Air Force's UK fleet of Hawk fast jet trainer aircraft continues through the long-term availability contract, along with support to users of Hawk trainer aircraft around the world.

The UK Combat Air Strategy, announced in the year, is a significant milestone for the Air sector and sends a strong signal of intent about the UK's commitment to retaining a leading position in Combat Air. The Tempest programme is a key enabler to deliver this strategy and the business is currently mobilising resources against a contract awarded in July, whilst also engaging with industry partners and the Ministry of Defence to define and mature the technologies and capabilities that are required.

US Programmes

Final price agreement was secured on F-35 Lot 11. Negotiations on Lots 12 to 14 are expected to conclude in the first half of 2019, which will enable an expected ramp-up to full-rate production by 2020. In the year, 110 rear fuselage assemblies were delivered for the Low-Rate Initial Production contracts across Lots 10, 11 and 12.

At RAF Marham in Norfolk, following acceptance of the Lightning Operating Centre, the UK's first four F-35 aircraft arrived in June, and a further five aircraft arrived during September, enabling the UK government to declare Initial Operational Capability in December. The integration of F-35 onto the Queen Elizabeth Aircraft Carrier has commenced, with the initial phase of First of Class Flight trials now complete.

During the second half of the year, contract award for the Performance Based Logistics arrangements for BAE Systems equipment responsibilities was achieved, underpinning a growing contribution by BAE Systems to the F-35 global fleet support.

Saudi Arabia

The Memorandum of Intent signed between the Kingdom of Saudi Arabia and the UK government in March 2018 continues to progress towards reaching an Agreement for a further 48 Typhoon aircraft, support and transfer of technology and capability. This will enable BAE Systems to continue with the Industrialisation of Defence capabilities in the Kingdom of Saudi Arabia. Final assembly of all 48 Typhoon aircraft will be In-Kingdom.

The Typhoon support contracts continue to operate well. Agreement has been reached with the Saudi Arabian government for BAE Systems to continue to provide Typhoon support services to the Royal Saudi Air Force against which we have booked order intake of £3.2bn in December 2018 for support services up to and including 2022.

The Royal Saudi Air Force will receive their first In-Kingdom final-assembled Hawk aircraft in early 2019. The company has delivered 14 of 22 major units on schedule, to meet this final assembly programme and first flight of a Hawk assembled in Saudi Arabia occurred in November.

The Royal Saudi Naval Forces accepted the third and final ship in the Minehunter mid-life update programme in April, with a training services contract signed in the year.

Work continues to reorganise our portfolio of interests in a number of industrial companies in Saudi Arabia. During the year Riyadh Wings Aviation Academy LLC increased its ownership to 11.85% in the Group's Overhaul and Maintenance Company (OMC) subsidiary, and is contracted to acquire a further interest up to 49%. OMC has disposed of its 85.7% shareholding in Aircraft Accessories and Components Company to Saudi Arabian Military Industries (SAMI) in 2019. These reorganisations are in support of our strategy to develop indigenous supply in Saudi Arabia through our In-Kingdom Industrial Participation programme, promoting training, development and employment opportunities in line with the Kingdom's National Transformation Plan and Vision 2030.

Through the restructuring of the Group's portfolio of interests in a number of Kingdom of Saudi Arabia industrial companies along with sustaining current industrialised capability and building on our strong history in Saudi Arabia, we are working in partnership to continue to deliver these priorities with the SAMI organisation to explore how we can collaborate to deliver further In-Kingdom Industrial Participation.

It should be recognised that the Group is reliant on the continued approval of export licences by a number of governments in order to continue supplies to the Kingdom of Saudi Arabia. Significant changes in the policies of such governments may affect the Group's own provision of capability to the country and it is liaising closely with the UK government in working to reduce the impact of any such occurrence.

Australia

In March, the Commonwealth of Australia agreed upgrade and sustainment contracts worth A$1.0bn (£0.6bn) for the Jindalee Operational Radar Network, to be delivered over an initial ten-year term. Mobilisation of the acquisition and support teams has been completed and support of all radar sites transferred to the business.

In June, the Commonwealth of Australia selected the Group as the preferred tenderer for the design and build of up to nine ships for the Hunter Class programme for the Royal Australian Navy. We subsequently agreed the contract and scope for the initial four-year design and productionisation phase with a value of A$1.9bn (£1.1bn). The production scope is to be negotiated in due course for the first batch of ships.

We have continued to provide in-service support to the Royal Australian Navy's two Landing Helicopter Docks under the support contract which was extended to run until June 2019. Trials have identified a number of areas where rectifications are in process, with final acceptance of the vessels under the acquisition contract expected in 2019. However, in December, the Commonwealth announced that we had not been selected for the next stage of Landing Helicopter Dock support.

Progress continues on the sustainment and upgrade of the Anzac fleet under the Warship Asset Management Alliance.

The Hawk Mk127 Lead-In Fighter project team continues to maintain the high level of aircraft availability required. The Capability Assurance Programme to upgrade the Hawk fleet to meet the F-35 training requirements remains on schedule.

Mobilisation activity for sustainment of the regional F-35 fleet continues to progress at our Williamtown facility, with the first two aircraft to be supported arriving in Australia in December.

We were notified in March 2018 that we had been unsuccessful in our bid for the Land 400 Phase 2 Combat Reconnaissance Vehicle programme.

MBDA

During the year MBDA secured new contracts for additional Taurus stand-off missiles in South Korea and for Marte Extended Range anti-ship missiles to Qatar. The contract for the supply of missiles to Qatar for the 24 Typhoon aircraft became effective in September.

MBDA also secured the development and manufacture of next generation MICA air-to-air missiles in France, and further five-year support to the Aster system in France, Italy and the UK.

An amended Request for Proposal was received for the proposed future German ground-based air defence system, TLVS. MBDA is partnered with Lockheed Martin on this opportunity.

MBDA made good progress on development programmes with key test firings successfully achieved in the year for both Sea Venom anti-ship and Land Ceptor air defence missiles.

The Sea Ceptor naval air defence missile system entered into service with the Royal Navy Type 23 frigates in May. Meteor entered into service with the Royal Air Force on Typhoon. The French Army introduced in operations the new fifth-generation land combat missile MMP.

Looking forward

Forward-looking information for the Air reporting segment is provided on page 39.

1. Including share of equity accounted investments.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.
4. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Segmental performance: Maritime

Maritime, with 16,000 employees[1], comprises the Group's UK-based maritime and land activities.

Operational and strategic key points

- HMS Queen Elizabeth has undergone successful initial F-35 Lightning II flight trials
- Cost growth on the Aircraft Carrier programme has resulted in a more conservative trading of contract profitability. Sea trials for HMS Prince of Wales are expected within the next year
- Type 26 selected as the design for the Canadian Surface Combatant programme
- Receipt of the full £1.6bn contract for the seventh Astute Class submarine, Agincourt, with order intake in the year of £0.7bn
- Further £1.3bn funding extension for the Dreadnought programme received
- Offshore Patrol Vessel programme quality issues have required the creation of a £47m loss provision
- Management strengthened across segment to focus on programme schedule, execution and cost performance
- CTA International, BAE Systems' joint venture with Nexter, delivered 115 40mm cased-telescopic cannons
- In January 2019, entered into an agreement with Rheinmetall to create a joint UK-based military land vehicle design, manufacturing and support business, subject to regulatory clearance

Financial performance

Financial performance measures as defined by the Group[2]

	2018	2017 (restated[4])
Order intake[1]	**£3,513m**	£4,671m
Order backlog[1]	**£9.0bn**	£8.5bn
Sales	**£2,975m**	£2,877m
Underlying EBITA	**£209m**	£251m
Return on sales	**7.0%**	8.7%
Operating business cash flow	**£67m**	£278m

Financial performance measures defined in IFRS[3]

	2018	2017 (restated[4])
Revenue	**£2,940m**	£2,845m
Operating profit	**£191m**	£240m
Return on revenue	**6.5%**	8.4%
Cash flow from operating activities	**£190m**	£396m

- Sales of £3.0bn are marginally higher than 2017. As expected, whilst the Dreadnought submarine and Type 26 programmes continue to ramp-up, activity levels on the Carrier programme are reducing.
- Return on sales for the year was at 7.0%. Further charges on the five-ship Offshore Patrol Vessels contract were taken and trading on the Carrier programme was at a more conservative level than planned. Performance in the submarines business was ahead of plan on improved milestone achievement and risk retirement.
- There was an operating cash inflow of £67m. Reported performance reflects the reversal of the £106m VAT timing benefit from last year.
- Order backlog increased to £9.0bn following the awards in the first half of the year for Astute Boat 7 pricing and further funding under the Dreadnought programme.

Operational performance

Naval Ships

On the aircraft carrier programme, large volume installation activities continue to progress on HMS Prince of Wales, with commissioning of systems continuing through 2019 and sea trials also scheduled to take place in 2019.

Work continues to support HMS Queen Elizabeth. Following the completion of a Capability Insertion Period, successful fixed wing flight trials took place in the second half of 2018, with the first F-35

Lightning II deck landing completed. However, cost growth on the programme has resulted in a more conservative trading of contract profitability in the period.

The first of the five Offshore Patrol Vessels, HMS Forth, completed sea trials in December 2017. However, quality issues have had to be resolved resulting in unanticipated programme cost growth and a £47m loss provision has been recorded in the year. Lessons learned are being applied to the other ships in build. Sea trials on the second ship, HMS Medway, took place in November 2018 and the ship is due to be delivered to the customer in the first quarter of 2019. Construction of the remaining three Offshore Patrol Vessels on the Clyde continues through 2019.

The three Type 26 ships continue in production. The programme currently employs over 1,500 people and activities have continued to build progressively during 2018 on transition from detailed design through to production readiness and the commencement of unit build.

Our Type 26 platform design has opened up opportunities abroad and in February 2019, the Canadian government, together with Irving Shipbuilding, selected Lockheed Martin Canada, using our Type 26 platform design, as subcontractor for the Canadian Surface Combatant programme. This is a further endorsement of the Global Combat Ship as one of the world's most advanced anti-submarine warships.

Submarines

The first three Astute Class submarines are in operational service with the Royal Navy. Progress continues on the manufacture of the remaining four boats. A full contract award for the seventh boat, Agincourt, was secured in March.

Functional and spatial design and production on the first of class continues to advance on the Dreadnought Class submarine programme, the replacement for the Vanguard Class submarines. Contract funding of £1.3bn was received through 2018.

The major programme of building works at the Barrow site continues, with contracts in place totalling more than £0.5bn.

The Dreadnought Alliance Agreement detailing the organisational, governance and commercial arrangements between the three parties, the Submarine Delivery Agency, BAE Systems and Rolls-Royce was agreed, allowing for the formal stand-up of the Alliance from April 2018.

Maritime Services

BAE Systems continues to manage and maintain HM Naval Base, Portsmouth, and supports more than half of the Royal Navy's surface fleet through the Maritime Support Delivery Framework contract. The Ministry of Defence extended this contract to March 2020 in the early part of the year.

During the second half of the year, we have mobilised the Type 45 Power Improvement Programme in collaboration with Cammell Laird and BMT, having been selected as prime contractor in the first half of 2018.

Progress continues on the £270m Spearfish torpedo programme, with the demonstration phase forecast to complete in 2020.

Maritime Services has delivered a transformation programme through 2018 to streamline its processes and ensure it is able to deliver value for money as we continue to provide the Royal Navy with the capability it needs to protect the nation's interests.

Land UK

The business continues to provide UK and international customers with a wide range of light and heavy munitions, and support to previously supplied armoured vehicles and bridging systems.

During the year, 115 40mm cased-telescopic cannons were delivered to the Ministry of Defence by CTA International, a joint venture between BAE Systems and Nexter, bringing cumulative deliveries to 275 of 515. This is the first entirely new medium-calibre cannon and ammunition system qualified by the British Army since the late 1960s. Also during the period an order for £72m was received to deliver 110 Case Telescoped Armament Systems to the French Army under their 6x6 combat armoured reconnaissance vehicle programme.

The business is one of two contenders delivering the design stages of the Challenger 2 Life Extension Programme and the British Army's bridging system.

In January 2019 the business entered into an agreement with Rheinmetall to create a joint UK-based military land vehicle design, manufacturing and support business. Rheinmetall will purchase a 55% stake in the existing BAE Systems UK-based combat vehicles business for £28.6m with BAE Systems retaining 45%. The transaction is subject to regulatory approvals which are anticipated to be completed in the first half of 2019. The transaction does not include Land UK's munitions business or its holding in the CTAI joint venture with Nexter.

Looking forward

Forward-looking information for the Maritime reporting segment is provided on page 39.

1. Including share of equity accounted investments.
2. For alternative performance measure definitions see glossary on page 12.
3. International Financial Reporting Standards.
4. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Segmental looking forward

Effective 1 January 2018, BAE Systems has five principal reporting segments, Electronic Systems, Cyber & Intelligence, Platforms & Services (US), Air and Maritime, which align with the strategic direction of the Group.

Electronic Systems

Electronic Systems comprises the US and UK-based electronics activities, including electronic warfare systems, electro-optical sensors, military and commercial digital engine and flight controls, precision guidance and seeker solutions, next-generation military communications systems and data links, persistent surveillance capabilities, and hybrid electric drive systems.

Electronic Systems is well positioned to address current and evolving priority programmes from its strong franchise positions in electronic warfare, precision guidance and seeker solutions. Electronic Systems has a long-standing programme of research and development, and its focus remains on maintaining a diverse portfolio of defence and commercial products and capabilities for US and international customers.

The business expects to benefit from its ability to apply innovative technology solutions that meet defence customers' changing requirements. As a result, the business is well positioned for the medium term with strong significant roles on F-35 Lightning II and classified programmes, as well as with specific products such as APKWS®. Over the longer term, the business is poised to leverage its technology strength in emerging areas of demand such as space resilience and autonomous vehicles.

In the commercial aviation market, Electronic Systems' technology innovations are enabling the business to maintain its long-standing customer positions and to compete for, and win, new business.

Cyber & Intelligence

Cyber & Intelligence comprises the US-based Intelligence & Security business and UK-headquartered Applied Intelligence business, and covers the Group's cyber security, secure government, and commercial and financial security activities.

Intelligence & Security

The outlook for the US government services sector is stable, although market conditions remain highly competitive and continue to evolve. The US business remains well positioned and will continue to leverage its established market positions and reputation for reliable and adaptable performance to meet customer demands for innovative, cost-effective and cyber-hardened solutions to pursue recompeted contracts and new business across its portfolio of sustainment, integration and modernisation solutions for military, intelligence and nuclear triad customers.

Applied Intelligence

Strong market demand and continued investment in people and products position the business for revenue growth in the medium term. Profitability is expected to continue to benefit from focus on operational efficiency and cost control.

Platforms & Services (US)

Platforms & Services (US), with operations in the US, UK and Sweden, manufactures combat vehicles, weapons and munitions, and delivers services and sustainment activities, including ship repair and the management of government-owned munitions facilities.

The combat vehicles business is underpinned by a growing order backlog and incumbencies on key franchise programmes. These include the US Army's Armored Multi-Purpose Vehicle, M109A7 self-propelled howitzer, Bradley upgrade programmes, the Amphibious Combat Vehicle; and the CV90 and BvS10 export programmes from our BAE Systems Hägglunds business.

FNSS continues to execute on its order book of both Turkish and international orders.

These long-term contracts and franchise positions make the combat vehicles business well placed for growth in the medium term, and the team is closely following the US Army's acquisition plans for its next generation of combat vehicles.

In the maritime domain, the sector has a strong position on naval gun programmes and US Navy ship repair activities where the business has invested in facilities in key homeports. This capitalised infrastructure represents a high barrier to entry, and the business remains well aligned to the US Navy's operational strategy.

The Group remains a leading provider of gun systems and precision strike capabilities and, in the complex ordnance manufacturing business, the business continues to manage and operate the US Army's Radford and Holston munitions facilities under previously awarded contracts.

Air

Air comprises the Group's UK-based air activities for European and International markets and US Programmes and its businesses in Saudi Arabia and Australia, together with its 37.5% interest in the European MBDA joint venture.

Future UK sales are underpinned by existing contracts for both Typhoon production and support. Production of rear fuselage assemblies for F-35 Lightning II will increase over the next two years to reach its expected peak rate for the next decade. The business plays a significant role in the F-35 sustainment programme in support of Lockheed Martin.

Defence and security remain priorities for the UK government, reaffirmed in the Modernising Defence Programme and the recently announced UK Combat Air Strategy, which provides the base to enable long-term planning and investment in a key strategic part of the business.

Discussions continue with current and prospective customers in relation to potential further contract awards for Typhoon and Hawk.

The UK Typhoon support operation is underpinned by a long-term partnering arrangement with the Ministry of Defence.

In Saudi Arabia, the In-Kingdom Industrial Participation programme continues to make good progress consistent with our long-term strategy, as well as the Saudi Arabian government's National Transformation Plan and Vision 2030. In order to provide ongoing capability to international customers, the company is reliant on the continued approval of export licences by a number of governments. Any significant change in UK or foreign government policy in this regard may have an adverse effect on the Group's provision of capability to the Kingdom of Saudi Arabia and the Group is liaising closely with the UK government in working to reduce the impact of any such occurrence.

The Australian business has long-term sustainment and upgrade activities in maritime, air, wide area surveillance, missile defence and electronic systems. It will expand into ship design and productionisation on the Hunter Class frigate programme from 2019.

MBDA has a strong order book which is driving increasing production and sales. Development programmes continue to improve the long-term capabilities of the business.

Maritime

Maritime comprises the Group's UK-based maritime and land activities.

Maritime

In Maritime, there remains pressure on the Royal Navy's near-term budgets and a highly-competitive environment in ship support and upgrade. Overall the outlook is stable based on the long-term contracted positions.

Within Submarines, the business is executing the Astute Class programme, with four boats still in build. On the Dreadnought programme manufacturing activities continue on the first of class boat. Investment continues in the Barrow facilities in order to provide the capabilities to deliver these long-term programmes through the next decade and beyond.

In shipbuilding, sales are underpinned by the contracts to manufacture the Queen Elizabeth Class aircraft carriers, Type 26 frigates and River Class Offshore Patrol Vessels.

The through-life support of surface ship platforms provides a sustainable business in technical services and mid-life upgrades.

Land UK

The Land UK business continues to deliver support to armoured vehicle and bridging systems in UK and international markets, munitions under the 15-year Munitions Acquisition Supply Solution partnering agreement secured in 2008 and 40mm cased-telescopic cannons for the UK and French armies.

In January 2019 BAE Systems entered into an agreement with Rheinmetall to create a joint UK-based military land vehicle design, manufacturing and support business. Rheinmetall will purchase a 55% stake in the existing BAE Systems UK-based combat vehicles business for £28.6m, with BAE Systems retaining 45%. The new business is well positioned to address the upcoming Challenger II upgrade programme.

Consolidated income statement

for the year ended 31 December

	Notes	2018 £m	2018 Total £m	2017 (restated[1]) £m	2017 (restated[1]) Total £m
Continuing operations					
Sales	2	**18,407**		18,487	
Deduct Share of sales by equity accounted investments	2	**(2,812)**		(2,534)	
Add Sales to equity accounted investments	2	**1,226**		1,271	
Revenue	2		**16,821**		17,224
Operating costs			**(15,514)**		(16,043)
Other income			**158**		131
Group operating profit			**1,465**		1,312
Share of results of equity accounted investments			**140**		107
Underlying EBITA	2	**1,928**		1,974	
Non-recurring items		**(154)**		(13)	
EBITA		**1,774**		1,961	
Amortisation of intangible assets		**(85)**		(86)	
Impairment of intangible assets		**(33)**		(384)	
Financial expense of equity accounted investments		**(13)**		(34)	
Taxation expense of equity accounted investments		**(38)**		(38)	
Operating profit	2		**1,605**		1,419
Financial income		**228**		416	
Financial expense		**(609)**		(762)	
Net finance costs	3		**(381)**		(346)
Profit before taxation			**1,224**		1,073
Taxation expense	4		**(191)**		(216)
Profit for the year			**1,033**		857
Attributable to:					
Equity shareholders			**1,000**		827
Non-controlling interests			**33**		30
			1,033		857
Earnings per share	5				
Basic earnings per share			**31.3p**		26.0p
Diluted earnings per share			**31.2p**		25.9p

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Consolidated statement of comprehensive income

for the year ended 31 December

	2018			2017 (restated[1])		
	Other reserves £m	**Retained earnings £m**	**Total £m**	Other reserves £m	Retained earnings £m	Total £m
Profit for the year	**–**	**1,033**	**1,033**	–	857	857
Other comprehensive income						
Items that will not be reclassified to the income statement:						
Subsidiaries:						
Remeasurements on retirement benefit schemes	**–**	**74**	**74**	–	2,056	2,056
Tax on items that will not be reclassified to the income statement	**–**	**5**	**5**	–	(481)	(481)
Equity accounted investments (net of tax)	**–**	**6**	**6**	–	52	52
Items that may be reclassified to the income statement:						
Subsidiaries:						
Currency translation on foreign currency net investments	**400**	**–**	**400**	(630)	–	(630)
Amounts (charged)/credited to hedging reserve	**(25)**	**–**	**(25)**	59	–	59
Tax on items that may be reclassified to the income statement	**5**	**–**	**5**	(11)	–	(11)
Equity accounted investments (net of tax)	**15**	**–**	**15**	(18)	–	(18)
Total other comprehensive income for the year (net of tax)	**395**	**85**	**480**	(600)	1,627	1,027
Total comprehensive income for the year	**395**	**1,118**	**1,513**	(600)	2,484	1,884
Attributable to:						
Equity shareholders	**391**	**1,085**	**1,476**	(595)	2,454	1,859
Non-controlling interests	**4**	**33**	**37**	(5)	30	25
	395	**1,118**	**1,513**	(600)	2,484	1,884

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers and to correct a prior year error in respect of the accounting valuation of a longevity swap held by one of the Group's defined benefit pension schemes. See note 11 for details regarding the restatement.

Consolidated statement of changes in equity

for the year ended 31 December

	Attributable to equity holders of BAE Systems plc						
	Issued share capital £m	Share premium £m	Other reserves £m	Retained earnings £m	Total £m	Non-controlling interests £m	Total equity £m
Balance at 1 January 2018 as originally presented	87	1,249	6,098	(2,693)	4,741	43	4,784
Restatement[1]	–	–	(8)	(21)	(29)	–	(29)
Restated total equity at 1 January 2018	87	1,249	6,090	(2,714)	4,712	43	4,755
Profit for the year	–	–	–	1,000	1,000	33	1,033
Total other comprehensive income for the year	–	–	391	85	476	4	480
Total comprehensive income for the year	–	–	391	1,085	1,476	37	1,513
Share-based payments (inclusive of tax)	–	–	–	63	63	–	63
Net sale of own shares	–	–	–	1	1	–	1
Ordinary share dividends	–	–	–	(703)	(703)	(28)	(731)
Partial disposal of shareholding in subsidiary undertaking	–	–	–	(3)	(3)	20	17
At 31 December 2018	**87**	**1,249**	**6,481**	**(2,271)**	**5,546**	**72**	**5,618**
Balance at 1 January 2017 as originally presented	87	1,249	6,685	(4,583)	3,438	26	3,464
Restatement[1]	–	–	–	47	47	–	47
Restated total equity at 1 January 2017	87	1,249	6,685	(4,536)	3,485	26	3,511
Profit for the year	–	–	–	827	827	30	857
Total other comprehensive income for the year	–	–	(595)	1,627	1,032	(5)	1,027
Total comprehensive income for the year	–	–	(595)	2,454	1,859	25	1,884
Share-based payments (inclusive of tax)	–	–	–	53	53	–	53
Net purchase of own shares	–	–	–	(1)	(1)	–	(1)
Ordinary share dividends	–	–	–	(684)	(684)	(8)	(692)
At 31 December 2017	87	1,249	6,090	(2,714)	4,712	43	4,755

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers and to correct a prior year error in respect of the accounting valuation of a longevity swap held by one of the Group's defined benefit pension schemes. See note 11 for details regarding the restatement.

Consolidated balance sheet

as at 31 December

	Notes	2018 £m	2017 (restated[1]) £m	2016 (restated[1]) £m
Non-current assets				
Intangible assets		**10,658**	10,378	11,264
Property, plant and equipment		**2,365**	2,230	2,098
Investment property		**98**	101	110
Equity accounted investments		**429**	322	250
Other investments		**13**	6	6
Other receivables		**352**	387	351
Retirement benefit surpluses	6	**308**	302	223
Other financial assets		**245**	226	345
Deferred tax assets		**702**	702	1,181
		15,170	14,654	15,828
Current assets				
Inventories		**774**	733	776
Trade, other and contract receivables		**5,177**	4,244	3,959
Current tax		**81**	20	5
Other financial assets		**166**	89	204
Cash and cash equivalents		**3,232**	3,271	2,769
Assets held for sale		**146**	26	2
		9,576	8,383	7,715
Total assets		**24,746**	23,037	23,543
Non-current liabilities				
Loans		**(3,514)**	(4,069)	(4,425)
Other payables		**(1,536)**	(1,723)	(1,040)
Retirement benefit obligations	6	**(4,240)**	(4,324)	(6,330)
Other financial liabilities		**(104)**	(133)	(102)
Deferred tax liabilities		**–**	(4)	(10)
Provisions		**(427)**	(435)	(392)
		(9,821)	(10,688)	(12,299)
Current liabilities				
Loans and overdrafts		**(785)**	(14)	–
Trade and other payables		**(7,740)**	(6,755)	(6,917)
Other financial liabilities		**(74)**	(104)	(212)
Current tax		**(334)**	(305)	(311)
Provisions		**(334)**	(400)	(291)
Liabilities held for sale		**(40)**	(16)	(2)
		(9,307)	(7,594)	(7,733)
Total liabilities		**(19,128)**	(18,282)	(20,032)
Net assets		**5,618**	4,755	3,511
Capital and reserves				
Issued share capital		**87**	87	87
Share premium		**1,249**	1,249	1,249
Other reserves		**6,481**	6,090	6,685
Retained earnings – deficit		**(2,271)**	(2,714)	(4,536)
Total equity attributable to equity holders of BAE Systems plc		**5,546**	4,712	3,485
Non-controlling interests		**72**	43	26
Total equity		**5,618**	4,755	3,511

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers and to correct a prior year error in respect of the accounting valuation of a longevity swap held by one of the Group's defined benefit pension schemes. See note 11 for details regarding the restatement.

Approved by the Board on 20 February 2019 and signed on its behalf by:

C N Woodburn
Chief Executive

P J Lynas
Group Finance Director

Consolidated cash flow statement

for the year ended 31 December

	Notes	2018 £m	2017 (restated[1]) £m
Profit for the year		**1,033**	857
Taxation expense		**191**	216
Research and development expenditure credits		**(27)**	(20)
Share of results of equity accounted investments		**(140)**	(107)
Net finance costs		**381**	346
Depreciation, amortisation and impairment		**411**	728
Gain on investment revaluation		**(7)**	–
Profit on disposal of property, plant and equipment, and investment property		**(18)**	(10)
Loss in respect of held for sale assets and business disposals		**9**	13
Cost of equity-settled employee share schemes		**64**	61
Movements in provisions		**(101)**	150
Decrease in liabilities for retirement benefit obligations		**(153)**	(138)
(Increase)/decrease in working capital:			
Inventories		**(16)**	(29)
Trade, other and contract receivables		**(757)**	(397)
Trade and other payables		**530**	454
Taxation paid		**(200)**	(227)
Net cash flow from operating activities		**1,200**	1,897
Dividends received from equity accounted investments		**57**	72
Interest received		**25**	23
Purchase of property, plant and equipment, and investment property		**(358)**	(389)
Purchase of intangible assets		**(139)**	(87)
Proceeds from sale of property, plant and equipment, and investment property		**34**	34
Proceeds from sale of intangible assets		**–**	1
Purchase of subsidiary undertakings		**–**	(3)
Purchase of equity accounted investment		**(2)**	–
Partial disposal of shareholding in subsidiary undertaking		**17**	–
Equity accounted investment funding		**(1)**	(3)
Cash and cash equivalents acquired with subsidiary undertakings		**14**	–
Cash flow in respect of held for sale assets and business disposals		**12**	(6)
Cash and cash equivalents disposed of with subsidiary undertakings		**–**	(2)
Net cash flow from investing activities		**(341)**	(360)
Interest paid		**(203)**	(204)
Net sale/(purchase) of own shares		**1**	(1)
Equity dividends paid	7	**(703)**	(684)
Dividends paid to non-controlling interests		**(28)**	(8)
Cash flow from matured derivative financial instruments (excluding cash flow hedges)		**6**	(83)
Cash flow from movement in cash collateral		**2**	(15)
Cash flow from repayment of loans		**(7)**	–
Net cash flow from financing activities		**(932)**	(995)
Net (decrease)/increase in cash and cash equivalents		**(73)**	542
Cash and cash equivalents at 1 January		**3,264**	2,771
Effect of foreign exchange rate changes on cash and cash equivalents		**41**	(49)
Cash and cash equivalents at 31 December		**3,232**	3,264
Comprising:			
Cash and cash equivalents		**3,232**	3,271
Overdrafts		**–**	(7)
Cash and cash equivalents at 31 December		**3,232**	3,264

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

Notes to the accounts

1. Preparation

Basis of preparation and statement of compliance

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

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

Changes in accounting policies

IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers became effective on 1 January 2018. The impact of adoption is set out in note 11.

IFRS 16 Leases will be effective from 1 January 2019. The expected impact of adoption is set out in note 12.

2. Segmental analysis

Sales and revenue by reporting segment[1]

	Sales		Deduct Share of sales by equity accounted investments		Add Sales to equity accounted investments		Revenue	
	2018 £m	2017 (restated[2]) £m	**2018 £m**	2017 (restated[2]) £m	**2018 £m**	2017 (restated[2]) £m	**2018 £m**	2017 (restated[2]) £m
Electronic Systems	**3,965**	3,598	**(101)**	(95)	**101**	95	**3,965**	3,598
Cyber & Intelligence	**1,678**	1,818	–	–	–	–	**1,678**	1,818
Platforms & Services (US)	**3,005**	2,951	**(141)**	(103)	–	–	**2,864**	2,848
Air	**6,712**	7,210	**(2,224)**	(2,006)	**1,091**	1,108	**5,579**	6,312
Maritime	**2,975**	2,877	**(37)**	(41)	**2**	9	**2,940**	2,845
HQ	**350**	336	**(309)**	(289)	–	–	**41**	47
	18,685	18,790	**(2,812)**	(2,534)	**1,194**	1,212	**17,067**	17,468
Intra-group sales/revenue	**(278)**	(303)	–	–	**32**	59	**(246)**	(244)
	18,407	18,487	**(2,812)**	(2,534)	**1,226**	1,271	**16,821**	17,224

Operating profit/(loss) by reporting segment[1]

	Underlying EBITA		Non-recurring items[3]		Amortisation and impairment of intangible assets[4]		Financial and taxation expense of equity accounted investments		Operating profit/(loss)	
	2018 £m	2017 (restated[2]) £m	**2018 £m**	2017 £m	**2018 £m**	2017 £m	**2018 £m**	2017 (restated[2]) £m	**2018 £m**	2017 (restated[2]) £m
Electronic Systems	**606**	541	**–**	–	**(16)**	(20)	**–**	–	**590**	521
Cyber & Intelligence	**111**	58	**–**	–	**(52)**	(419)	**–**	–	**59**	(361)
Platforms & Services (US)	**210**	237	**(40)**	(13)	**(8)**	(9)	**(1)**	(2)	**161**	213
Air	**859**	967	**–**	–	**(12)**	(8)	**(37)**	(41)	**810**	918
Maritime	**209**	251	**–**	–	**(16)**	(8)	**(2)**	(3)	**191**	240
HQ	**(67)**	(80)	**(114)**	–	**(14)**	(6)	**(11)**	(26)	**(206)**	(112)
	1,928	1,974	**(154)**	(13)	**(118)**	(470)	**(51)**	(72)	**1,605**	1,419
Net finance costs									**(381)**	(346)
Profit before taxation									**1,224**	1,073
Taxation expense									**(191)**	(216)
Profit for the year									**1,033**	857

1. Reporting segments have been re-presented to reflect the organisational changes which took effect on 1 January 2018.
2. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.
3. Non-recurring items in 2018 comprises a Guaranteed Minimum Pension equalisation charge of £114m, and a loss on disposal of the Mobile, Alabama, shipyard of £40m. Non-recurring items in 2017 represented a loss on the disposal of the BAE Systems San Francisco Ship Repair business.
4. The impairment of intangible assets in 2018 relates to Silversky customer-related intangibles in the Applied Intelligence business. In 2017 the charge represented the impairment of goodwill in Applied Intelligence.

3. Net finance costs

	2018 £m	2017 £m
Interest income	**26**	24
Gain on remeasurement of financial instruments at fair value through profit or loss[1]	**186**	54
Foreign exchange gains[2]	**16**	338
Financial income	**228**	416
Interest expense on bonds and other financial instruments	**(204)**	(202)
Facility fees	**(4)**	(4)
Net present value adjustments	**(31)**	(44)
Net interest expense on retirement benefit obligations	**(103)**	(165)
Loss on remeasurement of financial instruments at fair value through profit or loss[1]	**(40)**	(317)
Foreign exchange losses[2]	**(227)**	(30)
Financial expense	**(609)**	(762)
Net finance costs	**(381)**	(346)

1. Comprises gains and losses on derivative financial instruments, including derivative instruments to manage the Group's exposure to interest rate fluctuations on external borrowings and exchange rate fluctuations on balances with the Group's subsidiaries and equity accounted investments.
2. The foreign exchange gains and losses primarily reflect exchange rate movements on US dollar-denominated borrowings.

Additional analysis

	2018 £m	2017 £m
Net finance costs:		
Group	**(381)**	(346)
Share of equity accounted investments	**(13)**	(34)
	(394)	(380)
Analysed as:		
Underlying net interest expense[2]:		
Group	**(213)**	(226)
Share of equity accounted investments	**(2)**	(19)
	(215)	(245)
Other:		
Group:		
Net interest expense on retirement benefit obligations	**(103)**	(165)
Fair value and foreign exchange adjustments on financial instruments and investments[1]	**(65)**	45
Share of equity accounted investments:		
Net interest expense on retirement benefit obligations	**(3)**	(8)
Fair value and foreign exchange adjustments on financial instruments and investments	**(8)**	(7)
	(394)	(380)

1. The net loss (2017 gain) primarily reflects foreign exchange translational losses (2017 gains) on US dollar-denominated bonds held by BAE Systems plc.
2. Underlying net interest expense is defined as finance costs for the Group and its share of equity accounted investments, excluding net interest expense on retirement benefit obligations, and fair value and foreign exchange adjustments on financial instruments and investments.

4. Taxation expense

Reconciliation of taxation expense

The following table reconciles the theoretical income tax expense, using the UK corporation tax rate, to the reported tax expense. The reconciling items represent, besides the impact of tax rate differentials and changes, non-taxable benefits or non-deductible expenses arising from differences between the local tax base and the reported financial statements.

	2018 £m	2017 (restated[1]) £m
Profit before taxation	**1,224**	1,073
UK corporation tax rate	**19%**	19.25%
Expected income tax expense	**(233)**	(207)
Effect of tax rates in foreign jurisdictions, including US state taxes	**(43)**	(95)
Effect of intra-group financing	**14**	15
Expenses not tax effected	**(14)**	(8)
Income not subject to tax	**18**	46
Research and development tax credits and patent box benefits	**14**	18
Non-deductible goodwill impairment	**–**	(74)
Chargeable gains	**(1)**	(2)
Utilisation of previously unrecognised tax losses	**1**	3
Adjustments in respect of prior years	**37**	9
Adjustments in respect of equity accounted investments	**27**	21
Tax rate adjustment[2]	**5**	57
Other	**(16)**	1
Taxation expense	**(191)**	(216)

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.
2. 2017 included a £58m credit in respect of US tax reform enacted in December 2017.

Calculation of the underlying effective tax rate

	2018 £m	2017 (restated[1]) £m
Profit before taxation	**1,224**	1,073
Add back:		
Taxation expense of equity accounted investments	**38**	38
Goodwill impairment	**–**	384
Adjusted profit before taxation	**1,262**	1,495
Taxation expense	**(191)**	(216)
Taxation expense of equity accounted investments	**(38)**	(38)
Exclude: Impact of US tax reform enacted in December 2017	**–**	(58)
Adjusted taxation expense (including equity accounted investments)	**(229)**	(312)
Underlying effective tax rate	**18%**	21%

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.

5. Earnings per share

	2018			2017 (restated[1])		
	£m	**Basic pence per share**	**Diluted pence per share**	£m	Basic pence per share	Diluted pence per share
Profit for the year attributable to equity shareholders	**1,000**	**31.3**	**31.2**	827	26.0	25.9
Add back/(deduct):						
Amortisation and impairment of intangible assets, post tax[2]	**97**			68		
Impairment of goodwill	**–**			384		
Non-cash movements, being net interest expense on retirement benefit obligations, post tax[2]	**87**			137		
Non-cash movements, being fair value and foreign exchange adjustments on financial instruments and investments, post tax[2]	**60**			(30)		
Non-recurring items, post tax[2]	**126**			10		
Impact of US tax reform enacted in December 2017[3]	**–**			(58)		
Underlying earnings, post tax	**1,370**	**42.9**	**42.8**	1,338	42.1	41.9

		Millions	**Millions**		Millions	Millions
Weighted average number of shares used in calculating basic earnings per share		**3,192**	**3,192**		3,182	3,182
Incremental shares in respect of employee share schemes			**9**			15
Weighted average number of shares used in calculating diluted earnings per share			**3,201**			3,197

1. Prior year comparatives have been restated upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers. See note 11 for details regarding the restatement.
2. The tax impact is calculated using the underlying effective tax rate of 18% (2017 21%).
3. Prior year comparatives have been restated to exclude an additional £18m benefit in respect of the impact of US tax reform enacted in December 2017 resulting from the restatement of prior year comparatives upon the Group's adoption of IFRS 15 Revenue from Contracts with Customers.

6. Retirement benefits

Funding

Introduction

The majority of the UK and US defined benefit pension schemes are funded by the Group's subsidiaries and equity accounted investments. The individual pension schemes' funding requirements are based on actuarial measurement frameworks set out in their funding policies.

For funding valuation purposes, pension scheme assets are included at market value at the valuation date, whilst the liabilities are measured on an actuarial funding basis using the projected unit credit method and discounted to their present value based on prudent assumptions set by the trustees following consultation with scheme actuaries.

The funding valuations are performed by professionally qualified independent actuaries and include assumptions which differ from the actuarial assumptions used for IAS 19 accounting purposes shown on page 51. The purpose of the funding valuations is to design funding plans which ensure that the schemes have sufficient funds available to meet future benefit payments.

UK valuations

Funding valuations of the Group's nine UK defined benefit pension schemes are performed every three years. The latest valuations were performed as at 31 March 2017. The next funding valuations will have an effective date of no later than 31 March 2020.

In November 2017, the 2017 triennial funding valuations and, where necessary, deficit recovery plans were agreed with the trustees and certified by the scheme actuaries after consultation with the UK Pensions Regulator.

The results of the most recent triennial valuations are shown below:

	At 31 March 2017			
	Main Scheme £bn	2000 Plan £bn	Other £bn	Total £bn
Market value of assets	12.8	4.3	4.5	21.6
Present value of liabilities	(14.4)	(4.6)	(4.7)	(23.7)
Funding deficit	(1.6)	(0.3)	(0.2)	(2.1)
Percentage of accrued benefits covered by the assets at the valuation date	89%	93%	96%	91%

The valuations were determined using the following mortality assumptions:

	2017
Life expectancy of a male currently aged 65 (years)	86 – 89
Life expectancy of a female currently aged 65 (years)	88 – 90
Life expectancy of a male currently aged 45 (years)	88 – 92
Life expectancy of a female currently aged 45 (years)	91 – 93

The discount rate assumptions used in the 2017 valuations were based on prudent levels of expected returns for the assets held by the schemes, reflecting the planned investment strategies and maturity profiles of each scheme. The discount rates are curves which provide a different rate for each year into the future.

The inflation assumptions were derived using data from the Bank of England which is based on the difference between the yields on index-linked and fixed interest long-term government bonds. The inflation assumption is a curve which provides a different rate for each year into the future.

In aggregate, the net funding deficit across the UK schemes at 31 March 2017 was £2.1bn. The funding valuations resulted in a significantly lower deficit than under IAS 19, largely due to lower liabilities reflecting the higher discount rate assumption. Under IAS 19, the discount rate for accounting purposes is based on third-party AA corporate bond yields whereas, for funding valuation purposes, the discount rate is based on a prudent level of expected returns from the broader and mixed types of investments reflected in the schemes' investment strategies, which are expected overall to yield higher returns than bonds.

The agreements reached are underpinned by contingency plans, which include a commitment by the Group to a further £50m of deficit funding into the largest scheme prior to the next triennial valuation in the event that the scheme funding level was to fall below pre-determined parameters. In addition, the Group would be required to pay £187m across its schemes with deficits at the valuation date if the funding levels for those schemes were to fall significantly and were to remain at or below those levels for nine months.

There have been no changes to the contributions or benefits, as set out in the rules of the schemes, for pension scheme members as a result of the new funding valuations.

The results of future triennial valuations and associated funding requirements will be impacted by a number of factors, including the future performance of investment markets and anticipated members' longevity.

US valuations
The Group's US pension schemes are valued annually, with the latest valuations performed as at 1 January 2018.

Contributions
Under the terms of the trust deeds of the UK schemes, the Group is required to have a funding plan determined at the conclusion of the triennial funding valuations.

Equity accounted investments make regular contributions to the schemes in which they participate in line with the schedule of contributions and are allocated a share of deficit funding contributions.

In 2018, total employer contributions to the Group's pension schemes were £554m (2017 £433m), including amounts funded by equity accounted investments of £38m (2017 £31m), and included approximately £211m (2017 £209m) of deficit recovery payments in respect of the UK schemes and £119m (2017 £62m) in respect of the US schemes.

Deficit contributions will further increase in line with any percentage growth in dividend payments made by the Group. Under the deficit recovery plans, these annual payments would subsequently fall by approximately £50m in 2022 as the deficits on certain schemes are expected to be cleared. The annual payments are expected to end in 2026 when all deficits are projected to be cleared. Under the last agreement made in 2014, all scheme deficits were projected to be cleared in 2026.

In 2019, the Group expects that contributions to its UK pension schemes will be broadly in line with 2018, whilst contributions to its US pension schemes are expected to reduce.

IAS 19 accounting

Principal actuarial assumptions

The assumptions used are estimates chosen from a range of possible actuarial assumptions which, due to the long-term nature of the obligation covered, may not necessarily occur in practice.

	UK			US		
	2018	2017	2016	**2018**	2017	2016
Financial assumptions						
Discount rate – past service (%)	**2.9**	2.6	2.7	**4.2**	3.7	4.2
Discount rate – future service (%)	**3.0**	2.7	2.7	**4.2**	3.7	4.2
Retail Prices Index (RPI) inflation (%)	**3.1**	3.1	3.2	**n/a**	n/a	n/a
Rate of increase in salaries (%)	**3.1**	3.1	3.2	**n/a**	n/a	n/a
Rate of increase in deferred pensions (%)	**2.1/3.1**	2.1/3.1	2.2/3.2	**n/a**	n/a	n/a
Rate of increase in pensions in payment (%)	**1.6 – 3.7**	1.6 – 3.7	1.7 – 3.7	**n/a**	n/a	n/a
Demographic assumptions						
Life expectancy of a male currently aged 65 (years)	**86 – 88**	86 – 88	86 – 89	**87**	87	87
Life expectancy of a female currently aged 65 (years)	**88 – 90**	88 – 90	89 – 90	**89**	89	89
Life expectancy of a male currently aged 45 (years)	**88 – 90**	88 – 90	88 – 91	**87**	87	87
Life expectancy of a female currently aged 45 (years)	**90 – 91**	90 – 92	91 – 92	**89**	89	89

Deficit allocation

MBDA participates in the Group's defined benefit schemes and, as these are multi-employer schemes, the Group has allocated a share of the IAS 19 pension surpluses and deficits to MBDA based on the relative payroll contributions of active members, which is consistent with prior years. Whilst this methodology is intended to reflect a reasonable estimate of the share of the deficit, it may not accurately reflect the obligations of the participating employers.

In the event that an employer who participates in the Group's pension schemes fails or cannot be compelled to fulfil its obligations as a participating employer, the remaining participating employers are obliged to collectively take on its obligations. The Group considers the likelihood of this event arising as remote.

The Group's share of the IAS 19 pension deficit allocated to equity accounted investments is included in the balance sheet within equity accounted investments.

Guaranteed Minimum Pension equalisation

A UK High Court judgment was delivered on 26 October 2018 concerning gender equalisation for the effect of Guaranteed Minimum Pensions (GMPs) for occupational pension schemes. It is expected that the impact of GMP equalisation will be in the region of £121m based on an estimate as at 26 October 2018 for the UK schemes that were contracted out of the State Earnings Related Pension Scheme between 1990 and 1997. This has been treated for IAS 19 purposes as a plan amendment and resulted in an increase in the pension deficit in the balance sheet and a corresponding non-recurring past service cost in the income statement.

The Group has allocated a share of the past service cost to MBDA based on the relative payroll contributions of active members. The Group's share of the £121m is £110m in respect of the Group's subsidiaries, plus £4m for the Group's share of MBDA's allocation. The remaining £7m relates to the share allocated to other participating employers.

Summary of movements in retirement benefit obligations

	UK £m	US and other £m	Total £m
Total net IAS 19 deficit at 1 January 2018[1]	(3,788)	(566)	(4,354)
Actual return on assets excluding amounts included in net interest expense	(1,022)	(422)	(1,444)
Decrease in liabilities due to changes in financial assumptions	1,295	265	1,560
Decrease in liabilities due to changes in demographic assumptions	171	17	188
Experience losses	(176)	(17)	(193)
Contributions in excess of service cost	185	105	290
Past service cost – plan amendments	(131)	–	(131)
Net interest expense	(88)	(24)	(112)
Foreign exchange adjustments	–	(38)	(38)
Movement in US healthcare schemes	–	(2)	(2)
Total net IAS 19 deficit at 31 December 2018	**(3,554)**	**(682)**	**(4,236)**
Allocated to equity accounted investments	304	–	304
Group's share of net IAS 19 deficit excluding Group's share of amounts allocated to equity accounted investments at 31 December 2018	**(3,250)**	**(682)**	**(3,932)**

1. Prior year comparatives have been restated to correct a prior year error in respect of the accounting valuation of a longevity swap held by one of the Group's defined benefit pension schemes. See note 11 for details regarding the restatement.

Sensitivity analysis

The sensitivity information has been derived using scenario analysis from the actuarial assumptions as at 31 December 2018 as set out on page 51.

Financial assumptions

The estimated impact of changes in the discount rate and inflation assumptions on the defined benefit pension obligation, together with the estimated impact on scheme assets, is shown in the table below. The estimated impact on scheme assets takes into account the Group's risk management activities in respect of interest rate and inflation risk. The sensitivity analysis on the defined benefit obligation is measured on an IAS 19 accounting basis and, therefore, does not reflect the natural hedging in the discount rate used for funding valuation purposes.

	(Increase)/decrease in pension obligation[1] £bn	Increase/(decrease) in scheme assets[1] £bn
Discount rate:		
0.1 percentage point increase	0.5	(0.2)
0.1 percentage point decrease	(0.5)	0.2
Inflation:		
0.1 percentage point increase	(0.4)	0.2
0.1 percentage point decrease	0.4	(0.2)

1. Before allocation to equity accounted investments.

The sensitivity of the valuation of the liabilities to changes in the inflation assumption presented above assumes that a 0.1 percentage point change to expectations of future inflation results in a 0.1 percentage point change to all inflation-related assumptions (rate of increase in salaries, rate of increase in deferred pensions and rate of increase in pensions in payment) used to value the liabilities. However, upper and lower limits exist on the majority of inflation-related benefits such that a change in expectations of future inflation may not have the same impact on the inflation-related benefits, and hence will result in a smaller change to the valuation of the liabilities. Accordingly, extrapolation of the above results beyond the specific sensitivity figures shown may not be appropriate. To illustrate this, the (increase)/decrease in the defined benefit pension obligation resulting from larger changes in the inflation assumption would be as follows:

	(Increase)/decrease in pension obligation[1] £bn
Inflation:	
0.5 percentage point increase	(1.3)
0.5 percentage point decrease	1.3
1.0 percentage point increase	(2.8)
1.0 percentage point decrease	2.5

1. Before allocation to equity accounted investments.

Demographic assumptions

Changes in the life expectancy assumption, including the benefit of longevity swap arrangements, would have the following effect on the total net IAS 19 deficit:

	(Increase)/decrease in net deficit[1] £bn
Life expectancy:	
One-year increase	(1.1)
One-year decrease	1.1

1. Before allocation to equity accounted investments.

7. Equity dividends

	2018 £m	2017 £m
Prior year final 13.0p dividend per ordinary share paid in the year (2017 12.7p)	**415**	404
Interim 9.0p dividend per ordinary share paid in the year (2017 8.8p)	**288**	280
	703	684

After the balance sheet date, the directors proposed a final dividend of 13.2p per ordinary share. The dividend, which is subject to shareholder approval, will be paid on 3 June 2019 to shareholders registered on 23 April 2019. The ex-dividend date is 18 April 2019.

Shareholders who do not at present participate in the Company's Dividend Reinvestment Plan and wish to receive the final dividend in shares rather than cash should complete a mandate form for the Dividend Reinvestment Plan and return it to the registrars no later than 10 May 2019.

8. Fair value measurement

Fair value of financial instruments

Certain of the Group's financial instruments are held at fair value.

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 money market funds are calculated by multiplying the net asset value per share by the investment held at the balance sheet date.

Due to the variability of the valuation factors, the fair values presented at 31 December may not be indicative of the amounts the Group would expect to realise in the current market environment.

Fair value hierarchy

The fair value measurement hierarchy is as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 – Inputs for the asset or liability that are not based on observable market data (i.e. unobservable inputs).

Carrying amounts and fair values of certain financial instruments

	2018		2017	
	Carrying amount £m	**Fair value £m**	Carrying amount £m	Fair value £m
Financial instruments measured at fair value:				
Non-current				
Available for sale	**–**	**–**	6	6
Equity investments at fair value through profit and loss	**13**	**13**	–	–
Other financial assets	**245**	**245**	226	226
Other financial liabilities	**(104)**	**(104)**	(133)	(133)
Current				
Other financial assets	**166**	**166**	89	89
Money market funds	**908**	**908**	899	899
Other financial liabilities	**(74)**	**(74)**	(104)	(104)
Financial instruments not measured at fair value:				
Non-current				
Loans[1]	**(3,514)**	**(3,597)**	(4,069)	(4,478)
Current				
Cash and cash equivalents (excluding money market funds)	**2,324**	**2,324**	2,372	2,372
Loans and overdrafts	**(785)**	**(794)**	(14)	(14)

1. US$500m of the US$800m 3.8% bond, repayable 2024, has been converted to a floating rate bond by utilising interest rate swaps. These derivatives have been designated as fair value hedges. Changes in the fair value of the bond attributable to interest rate risk, and gains and losses on the derivatives are recognised in the income statement. The bond has been included in financial instruments not measured at fair value because its carrying value has only been adjusted for the fair value attributable to interest rate risk on a portion of the bond, which has been calculated by discounting the future cash flows and translating at the appropriate balance sheet rate.

All of the financial assets and liabilities measured at fair value are classified as level 2 using the fair value hierarchy, except for money market funds, which are classed as level 1. There were no transfers between levels during the year.

Financial assets and liabilities in the Group's Consolidated balance sheet are either held at fair value or their carrying value approximates to fair value, with the exception of loans, most of which are held at amortised cost. The fair value of loans presented in the table above is derived from market prices.

9. Financial risk management

Currency risk

The Group's objective is to reduce its exposure to transactional volatility in earnings and cash flows from movements in foreign currency exchange rates, mainly the US dollar, euro, Saudi riyal and Australian dollar.

The Group is exposed to movements in foreign currency exchange rates in respect of foreign currency denominated transactions. All material firm transactional exposures are hedged using foreign exchange forward contracts and the Group aims, where possible, to apply cash flow hedge accounting to these transactions.

The Group is exposed to movements in foreign currency exchange rates in respect of the translation of net assets and income statements of foreign subsidiaries and equity accounted investments. The Group does not hedge the translation effect of exchange rate movements on the income statements or balance sheets of foreign subsidiaries and equity accounted investments it regards as long-term investments.

The estimated impact on foreign exchange gains and losses in net finance costs of a ten cent movement in the closing Sterling to US dollar exchange rate on the retranslation of US dollar-denominated bonds held by BAE Systems plc is approximately £56m (2017 £49m).

10. Related party transactions

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

	Year ended 31 December 2018 £m	Year ended 31 December 2017 £m
Sales to related parties	**1,226**	1,271
Purchases from related parties	**410**	425

	31 December 2018 £m	31 December 2017 £m
Amounts owed by related parties	**71**	90
Amounts owed to related parties[1]	**965**	938

1. At 31 December 2018, £869m (2017 £884m) was owed by BAE Systems plc and £96m (2017 £54m) by other Group subsidiaries.

11. Changes in accounting policies and restatements

This note explains the impact of changes in accounting policies and the correction of a prior year error on the Group's financial statements.

Impact on financial statements

As a result of changes in the Group's accounting policies, prior year comparative information has been restated for the adoption of IFRS 15 Revenue from Contracts with Customers. IFRS 9 Financial Instruments was adopted without restating comparative information.

Following an internal review of the third-party accounting valuation of a longevity swap held by one of the Group's pension schemes, the Group became aware of an error in respect of the treatment of experience collateral in the accounting valuation. This resulted in a material error in the value of pension scheme assets included in the financial statements for the years ended 31 December 2017 and 31 December 2016. This error has been corrected retrospectively by restating the comparative amounts presented in these financial statements.

The following tables show the adjustments recognised for each individual line item. Line items that are not affected by the changes have not been included. As a result, the sub-totals and totals disclosed cannot be recalculated from the numbers provided.

Consolidated balance sheet (extract)

	As at 31 December 2017			
	As previously reported £m	Impact of IFRS 15 £m	Valuation of longevity swap £m	Restated £m
Non-current assets				
Equity accounted investments	384	(60)	(2)	322
Deferred tax assets	724	(40)	18	702
	14,738	**(100)**	**16**	**14,654**
Current assets				
Inventories	723	10	–	733
Trade and other receivables including amounts due from customers for contract work	3,586	(3,586)	–	–
Trade, other and contract receivables	–	4,244	–	4,244
	7,715	**668**	**–**	**8,383**
Total assets	**22,453**	**568**	**16**	**23,037**
Non-current liabilities				
Trade and other payables	(1,722)	(1)	–	(1,723)
Retirement benefit obligations	(4,222)	–	(102)	(4,324)
Provisions	(413)	(22)	–	(435)
	(10,563)	**(23)**	**(102)**	**(10,688)**
Current liabilities				
Trade and other payables	(6,322)	(433)	–	(6,755)
Provisions	(345)	(55)	–	(400)
	(7,106)	**(488)**	**–**	**(7,594)**
Total liabilities	**(17,669)**	**(511)**	**(102)**	**(18,282)**
Net assets	**4,784**	**57**	**(86)**	**4,755**
Capital and reserves				
Other reserves	6,098	(8)	–	6,090
Retained earnings	(2,693)	65	(86)	(2,714)
Total equity attributable to equity holders of BAE Systems plc	**4,741**	**57**	**(86)**	**4,712**
Non-controlling interests	**43**	**–**	**–**	**43**
Total equity	**4,784**	**57**	**(86)**	**4,755**

Consolidated balance sheet (extract)

	As at 31 December 2016			
	As previously reported £m	Impact of IFRS 15 £m	Valuation of longevity swap £m	Restated £m
Non-current assets				
Equity accounted investments	299	(48)	(1)	250
Deferred tax assets	1,251	(79)	9	1,181
	15,947	**(127)**	**8**	**15,828**
Current assets				
Inventories	744	32	–	776
Trade and other receivables including amounts due from customers for contract work	3,305	(3,305)	–	–
Trade, other and contract receivables	–	3,959	–	3,959
	7,029	**686**	**–**	**7,715**
Total assets	**22,976**	**559**	**8**	**23,543**
Non-current liabilities				
Trade and other payables	(1,027)	(13)	–	(1,040)
Retirement benefit obligations	(6,277)	–	(53)	(6,330)
Provisions	(372)	(20)	–	(392)
	(12,213)	**(33)**	**(53)**	**(12,299)**
Current liabilities				
Trade and other payables	(6,540)	(377)	–	(6,917)
Provisions	(234)	(57)	–	(291)
	(7,299)	**(434)**	**–**	**(7,733)**
Total liabilities	**(19,512)**	**(467)**	**(53)**	**(20,032)**
Net assets	**3,464**	**92**	**(45)**	**3,511**
Capital and reserves				
Retained earnings	(4,583)	92	(45)	(4,536)
Total equity attributable to equity holders of BAE Systems plc	**3,438**	**92**	**(45)**	**3,485**
Non-controlling interests	**26**	**–**	**–**	**26**
Total equity	**3,464**	**92**	**(45)**	**3,511**

Consolidated income statement

	Year ended 31 December 2017 As previously reported £m	Impact of IFRS 15 £m	Restated on adoption of IFRS 15 £m
Continuing operations			
Sales	19,626	(1,139)	**18,487**
Deduct Share of sales by equity accounted investments	(2,575)	41	**(2,534)**
Add Sales to equity accounted investments	1,271	–	**1,271**
Revenue	18,322	(1,098)	**17,224**
Operating costs	(17,089)	1,046	**(16,043)**
Other income	131	–	**131**
Group operating profit	1,364	(52)	**1,312**
Share of results of equity accounted investments	116	(9)	**107**
Underlying EBITA	2,034	(60)	**1,974**
Non-recurring items	(13)	–	**(13)**
EBITA	2,021	(60)	**1,961**
Amortisation of intangible assets	(86)	–	**(86)**
Impairment of intangible assets	(384)	–	**(384)**
Financial expense of equity accounted investments	(34)	–	**(34)**
Taxation expense of equity accounted investments	(37)	(1)	**(38)**
Operating profit	1,480	(61)	**1,419**
Financial income	416	–	**416**
Financial expense	(762)	–	**(762)**
Net finance costs	(346)	–	**(346)**
Profit before taxation	1,134	(61)	**1,073**
Taxation expense	(250)	34	**(216)**
Profit for the year	884	(27)	**857**
Attributable to:			
Equity shareholders	854	(27)	**827**
Non-controlling interests	30	–	**30**
	884	(27)	**857**
Earnings per share			
Basic earnings per share	26.8p	(0.8)p	**26.0p**
Diluted earnings per share	26.7p	(0.8)p	**25.9p**
Underlying earnings per share[1]	43.5p	(1.4)p	**42.1p**

1. Restated underlying earnings per share excludes an additional £18m benefit in respect of the impact of US tax reform enacted in December 2017 included in the restated taxation expense above.

Consolidated statement of comprehensive income

	Year ended 31 December 2017			
	As previously reported £m	Impact of IFRS 15 £m	Valuation of longevity swap £m	Restated £m
Profit for the year	884	(27)	–	857
Other comprehensive income				
Items that will not be reclassified to the income statement:				
Subsidiaries:				
Remeasurements on retirement benefit schemes	2,105	–	(49)	2,056
Tax on items that will not be reclassified to the income statement	(490)	–	9	(481)
Equity accounted investments (net of tax)	53	–	(1)	52
Items that may be reclassified to the income statement:				
Subsidiaries:				
Currency translation on foreign currency net investments	(625)	(5)	–	(630)
Amounts credited to hedging reserve	59	–	–	59
Tax on items that may be reclassified to the income statement	(11)	–	–	(11)
Equity accounted investments (net of tax)	(15)	(3)	–	(18)
Other comprehensive income for the year (net of tax)	**1,076**	**(8)**	**(41)**	**1,027**
Total comprehensive income for the year	**1,960**	**(35)**	**(41)**	**1,884**
Attributable to:				
Equity shareholders	1,935	(35)	(41)	1,859
Non-controlling interests	25	–	–	25
	1,960	**(35)**	**(41)**	**1,884**

IFRS 9 Financial instruments – impact of adoption

IFRS 9 replaces the provisions of IAS 39 that relate to recognition, classification and measurement of financial assets and financial liabilities, de-recognition of financial instruments, impairment of financial assets and hedge accounting. The adoption of IFRS 9 Financial Instruments from 1 January 2018 resulted in changes in accounting policies; however, no adjustments were required to the amounts recognised in the financial statements in previous periods.

Classification and measurement

On 1 January 2018, the Group has classified its financial instruments in the appropriate IFRS 9 categories.

The derivative financial instruments designated as cash flow hedges and fair values hedges under IAS 39 at 31 December 2017 continue to qualify for hedge accounting under IFRS 9 at 1 January 2018 and are therefore treated as continuing hedges.

Derivative financial instruments that were not designated as hedges under IAS 39 were classified in the fair value through profit or loss category and gains and losses were recognised in the income statement in the period. There is no change to the classification of these financial instruments under IFRS 9 as they fail the contractual cash flow characteristics test in IFRS 9 (4.1.2(b)) and (4.1.2A(b)).

Trade receivables and amounts owed by equity accounted investments, previously classified in the loans and receivables category and measured at amortised cost under IAS 39, continue to be classified in the amortised cost category under IFRS 9 as they are held within a business model to collect contracted cash flows and these cash flows consist solely of payments of principal and interest.

Money market funds, previously classified in the available for sale category under IAS 39, were previously measured at fair value with any change in fair value recognised in other comprehensive income. Under IFRS 9, money market funds are measured at fair value through profit and loss. However, fair value approximates to amortised cost for these financials assets; therefore the impact on transition to IFRS 9 is immaterial. Money market funds continue to be presented within cash and cash equivalents in the Consolidated balance sheet.

Equity investments previously classified in the available for sale category under IAS 39 were previously measured at fair value with any change in fair value recognised in other comprehensive income. Under IFRS 9, equity investments are measured at fair value through profit and loss.

Impairment of financial assets

The Group has three types of financial assets that are subject to IFRS 9's new expected credit loss model: trade receivables, contract receivables and amounts owed by equity accounted investments.

Trade receivables and contract receivables do not contain a significant financing element and therefore expected credit losses are measured using the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognised from the initial recognition of the receivables.

The Group has assessed credit risk in relation to defence-related sales to government customers or sub-contractors to governments and believes it to be extremely low as the probability of default is insignificant; therefore the provision for expected credit losses is immaterial in respect of receivables from these customers. The Group considers expected credit losses for non-government commercial customers, however this risk is not material to the financial statements.

Amounts due from equity accounted investments primarily relate to trading balances with no significant financing element, in accordance with IFRS 15. The simplified approach is therefore used for these balances. The identified impairment loss was immaterial.

While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial.

There was minimal IFRS 9 impact on retained earnings at 1 January 2018 and therefore no restatement was required.

IFRS 15 Revenue from Contracts with Customers – impact of adoption

The Group has adopted IFRS 15 fully retrospectively in accordance with paragraph C3(a). Comparatives for the year ended 31 December 2017 have been restated. The following expedients have been used in accordance with paragraph C5:

– revenue in respect of completed contracts that begin and end in the same accounting period has not been restated;
– revenue in respect of completed contracts with variable consideration reflects the transaction price at the date the contracts were completed; and
– the transaction price allocated to unsatisfied and partially unsatisfied performance obligations as at 31 December 2017 is not disclosed.

As a result of the adoption of IFRS 15 Revenue from Contracts with Customers from 1 January 2018, the following adjustments were made to restate the amounts recognised in the balance sheet at 31 December 2017:

	As at 31 December 2017			
	As previously reported £m	Reclassification £m	Remeasurement £m	Restated on adoption of IFRS 15 £m
Equity accounted investments	384	–	(60)	324
Deferred tax assets	724	–	(40)	684
Inventories	723	10	–	733
Trade and other receivables including amounts due from customers for contract work	3,586	(3,586)	–	–
Trade, other and contract receivables	–	4,055	189	4,244
Non-current other payables	(1,722)	22	(23)	(1,723)
Current trade and other payables	(6,322)	(424)	(9)	(6,755)
Non-current provisions	(413)	(22)	–	(435)
Current provisions	(345)	(55)	–	(400)

The impact of adoption of the Group's retained earnings at 31 December 2017 and 31 December 2016 is as follows:

	2017 £m	2016 £m
Retained earnings – as previously reported	**(2,693)**	**(4,583)**
Recognition of revenue for over time contracts based on costs incurred and including attributable margin	201	259
Equity accounted investments – separation of development and production margin, net of tax	(59)	(48)
Licence revenue – deferral of revenue over the licence term	(32)	(39)
Deferred tax	(45)	(80)
Adjustment to retained earnings upon adoption of IFRS 15	65	92
Retained earnings – IFRS 15 (restated)	**(2,628)**	**(4,491)**

12. Adoption of IFRS 16 Leases

IFRS 16 is effective from 1 January 2019 and replaces IAS 17 Leases and related interpretations. It will result in almost all leases being recognised on the balance sheet by lessees, as the distinction between operating and finance leases is removed. Under the new standard, a right-of-use asset and a financial liability for future lease payments are recognised. The only exceptions are short-term leases, low-value leases, and leases of intangible assets.

The Group will apply the Standard from 1 January 2019. The Group has applied the modified retrospective transition approach and will not restate comparative amounts for the year ended 31 December 2018. In the majority of cases the Group has elected to measure right-of-use assets at the amount of the lease liability on adoption (adjusted for any lease prepayments or accrued lease expenses, onerous lease provisions, and leased assets which have subsequently been sub-leased). For a number of property leases the Group has elected to measure the right-of-use asset as if IFRS 16 had been applied since the start of the lease, but using the incremental borrowing rate at 1 January 2019, with the difference between the right-of-use asset and the lease liability taken to retained earnings.

The Group has elected to adopt the following practical expedients on transition:

– not to capitalise a right-of-use lease asset or related lease liability where the lease expires before 31 December 2019;
– not to reassess contracts to determine if the contract contains a lease and not to separate lease and non-lease elements;
– where an onerous lease provision is in existence, to utilise this provision to reduce the right-of-use asset value rather than undertaking an impairment review;
– to use hindsight in determining the lease term;
– to exclude initial direct costs from the measurement of the right-of-use asset; and
– to apply the portfolio approach where a group of leases has similar characteristics.

Impact of adoption of IFRS 16 Leases

Balance sheet

Upon transition on 1 January 2019, the Group will recognise a right-of-use lease asset of £1,300m (after adjustments for onerous lease provisions, lease prepayments and accrued lease expenses at 31 December 2018), and lease liabilities of £1,486m (non-current £1,270m; current £216m), along with a deferred tax asset of £2m. A sub-lease finance receivable of £70m will also be recognised. A transition adjustment of £92m will be recognised as a debit to retained earnings. The Group will not capitalise low-value leases on transition, or those which expire before 31 December 2019, and has opted not to apply IFRS 16 to leases relating to intangible assets. The right-of-use asset principally consists of property.

Income statement

Under IFRS 16 the Group will see a different pattern of expense within the income statement, as the IAS 17 operating lease expense is replaced by depreciation and interest charges. In 2019, the Group's EBITA metric will improve by an estimated £50m under IFRS 16 as the new depreciation expense is expected to be lower than the IAS 17 operating lease charge; however the new finance costs are expected to broadly offset this, such that net profit after tax and the underlying earnings metric are not expected to be materially different compared to the previous IAS 17 reporting basis.

Cash flow statement

The change in presentation as a result of the adoption of IFRS 16 will see an improvement in 2019 of an estimated £46m in cash flow generated from operating activities, offset by a corresponding decline in cash flow from financing activities. There is no overall cash flow impact from the adoption of the new Standard.

Lessor accounting under IFRS 16 is largely unchanged from IAS 17.

Estimated 2019 IFRS 16 leases impact on underlying EBITA by segment

	£m
Electronic Systems	4
Cyber & Intelligence	3
Platforms & Services (US)	3
Air	19
Maritime	2
HQ	19
Group	**50**

Impact on Consolidated balance sheet at 1 January 2019 (extract)

The following table shows the effect of adopting IFRS 16 on the Consolidated balance sheet at 1 January 2019.

	£m
Non-current assets	
Right-of-use assets	1,255
Investment property	45
Equity accounted investments	(11)
Finance lease receivable	61
Deferred tax assets	2
	1,352
Current assets	
Finance lease receivable	9
Trade, other and contract receivables	(26)
	(17)
Total assets	**1,335**
Non-current liabilities	
Lease liabilities	(1,270)
Provisions	24
	(1,246)
Current liabilities	
Lease liabilities	(216)
Trade and other payables	28
Provisions	7
	(181)
Total liabilities	**(1,427)**
Net assets	**(92)**
Capital and reserves	
Retained earnings	(92)
Total equity attributable to equity holders of BAE Systems plc	**(92)**
Non-controlling interests	–
Total equity	**(92)**

13. Annual General Meeting

This year's Annual General Meeting will be held on 9 May 2019. Details of the resolutions to be proposed at that meeting will be included in the notice of Annual General Meeting that will be sent to shareholders at the end of March 2019.

14. Other information

The financial information for the year ended 31 December 2018 contained in this preliminary announcement was approved by the Board on 20 February 2019. This announcement does not constitute statutory accounts of the Company within the meaning of Section 435 of the Companies Act 2006, but is derived from those accounts.

Statutory accounts for the year ended 31 December 2017 have been delivered to the Registrar of Companies. Statutory accounts for the year ended 31 December 2018 will be delivered to the Registrar of Companies following the Company's Annual General Meeting.

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