

Group financial highlights

We monitor the underlying financial performance of the Group using alternative performance measures. These measures are not defined in IFRS¹ and, therefore, are considered to be non-GAAP² measures. Accordingly, the relevant IFRS¹ measures are also presented where appropriate.

- Sales increased by £0.6bn to £19.6bn largely reflecting currency translation.
- Underlying EBITA increased to £2,034m, a 4% increase on a constant currency basis³.
- Underlying earnings per share increased by 8% to 43.5p.
- Operating business cash flow increased by £748m to £1,752m.
- Net debt reduced by £790m compared with 31 December 2016.
- Order intake⁴ of £20.3bn.
- Order backlog⁴ of £41.2bn was unchanged on a constant currency basis³.

Financial performance measures as defined by the Group

Sales

KPI

£19,626m

(2016 £19,020m)

Definition Revenue plus the Group's share of revenue of equity accounted investments.

Purpose Allows management to monitor the sales performance of subsidiaries and equity accounted investments.

Net debt

BONUS

KPI

£(752)m

(2016 £(1,542)m)

Definition Cash and cash equivalents, less loans and overdrafts (including debt-related derivative financial instruments).

Purpose Allows management to monitor the indebtedness of the Group.

Underlying EBITA

KPI

£2,034m

(2016 £1,905m)

Definition Operating profit excluding amortisation and impairment of intangible assets, finance costs and taxation expense of equity accounted investments (EBITA), and non-recurring items⁵.

Purpose Provides a measure of operating profitability that is comparable over time.

Order intake⁴

BONUS

KPI

£20,257m

(2016 £22,443m)

Definition Funded orders received from customers including the Group's share of order intake of equity accounted investments.

Purpose Allows management to monitor the order intake of subsidiaries and equity accounted investments.

Underlying earnings per share

BONUS

KPI

43.5p

(2016 40.3p)

Definition Basic earnings per share excluding amortisation and impairment of intangible assets, non-cash finance movements on pensions and financial derivatives, non-recurring items⁵ and, in 2017, a credit in respect of US tax reform enacted in December 2017.

Purpose Provides a measure of underlying performance that is comparable over time.

Order backlog⁴

£41.2bn

(2016 £42.0bn)

Definition 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.

Purpose Supports future years' sales performance of subsidiaries and equity accounted investments.

Operating business cash flow

KPI

£1,752m

(2016 £1,004m)

Definition Net cash flow from operating activities excluding taxation and including net capital expenditure, financial investment and dividends from equity accounted investments.

Purpose Allows management to monitor the operational cash generation of the Group.

KPI

References to Key Performance Indicators (KPIs) throughout the Annual Report.

BONUS

80% of the UK executive directors' bonuses are based on the achievement of financial KPIs (see page 101).

Group financial review

We monitor the underlying financial performance of the Group using the alternative performance measures defined on page 6. These measures are not defined in IFRS¹ and, therefore, are considered to be non-GAAP² measures. Accordingly, the relevant IFRS¹ measures are also presented where appropriate.

Peter Lynas Group Finance Director



Financial performance

Measures as defined by the Group

Sales \uparrow ₂₈

KPI

£19,626m (2016 £19,020m)

Underlying EBITA \uparrow ₂₈

KPI

£2,034m (2016 £1,905m)

Underlying earnings per share \uparrow ₃₀

KPI

BONUS

43.5p (2016 40.3p)

Operating business cash flow \uparrow ₃₁

KPI

£1,752m (2016 £1,004m)

Net debt \uparrow ₃₂

KPI

BONUS

£(752)m (2016 £(1,542)m)

Order intake³ \uparrow ₃₀

KPI

BONUS

£20,257m (2016 £22,443m)

Order backlog³ \uparrow ₃₀

£41.2bn (2016 £42.0bn)

Measures defined in IFRS¹

Revenue \uparrow ₂₈

£18,322m (2016 £17,790m)

Operating profit \uparrow ₂₈

£1,480m (2016 £1,742m)

Basic earnings per share \uparrow ₃₀

26.8p (2016 28.8p)

Net cash flow from operating activities \uparrow ₃₁

£1,897m (2016 £1,229m)

Income statement

Sales increased by £0.6bn to £19.6bn (2016 £19.0bn) largely reflecting currency translation.

Underlying EBITA increased by £129m to £2,034m (2016 £1,905m), giving a return on sales of 10.4% (2016 10.0%). There was an exchange translation benefit of £50m. Growth on a constant currency basis⁴ was at 4%.

Revenue increased by £0.5bn to £18.3bn (2016 £17.8bn) largely reflecting currency translation.

Operating profit decreased by £262m to £1,480m (2016 £1,742m). 2017 includes a £384m impairment in respect of the Applied Intelligence business, which is excluded from underlying EBITA. There was an exchange translation benefit of £39m.

Non-recurring items in 2017 of £13m represents a loss on the disposal of the BAE Systems San Francisco Ship Repair business. Non-recurring items in 2016 of £12m represented an impairment taken in respect of that business.

Amortisation of intangible assets is in line with the prior year at £86m (2016 £87m).

Impairment of goodwill in 2017 represents the impairment of goodwill in Applied Intelligence reflecting the future level and timing of expected returns from the business.

³ 80% of the UK executive directors' bonuses are based on the achievement of financial KPIs (see page 101).

Health and safety

Our collective focus on employee wellbeing and the health and safety of employees and those who work on, or visit, our sites is a contributory factor to the success of our organisation. Our safety culture and our employees demand high standards for all aspects of health and safety. This is supported both by our mandated Health and Safety Policy and the principles contained within our Code of Conduct for employees.

Employee wellbeing

We promote wellbeing through a wide variety of programmes, ranging from exercise and fitness promotion to occupational health checks. We know that good mental and physical health contributes to better decision-making, greater productivity and higher levels of employee satisfaction. We run campaigns to encourage employees to take responsibility for their health problems, such as heart disease, diabetes and cancer. Our Employee Assistance Programme is a confidential service available to employees and includes support and advice on personal matters.

Safety

Our business is highly complex and our employees are exposed to many risks. These range from slips, trips and falls in an office environment, confined space working and machinery hazards within manufacturing to fire and explosion risks associated with the manufacture and storage of munitions. Many of our employees operate heavy equipment, work at height or do physically demanding work in high-risk environments.

In order to ensure consistency, all businesses are required to comply with our Health and Safety Policy, which outlines and prescribes the responsibilities and arrangements in place for ensuring safety. It is the responsibility of individual business leaders to ensure that their organisations comply with the policy. We aim to mitigate or manage safety risks by finding new ways to enhance safety standards, increase awareness and continually drive a strong safety culture.

Due to the varied risk profiles and work environments within the Group, we operate safety management systems within each business, many of which are externally accredited to the OHSAS¹ 18001 standard. These systems identify and control risk, and are used to assure that processes and procedures are protecting our people and others who may be affected by our operations. Teams of safety specialists assist management in ensuring safety management systems are effective and that operational control of risk is maintained. Health and safety specialists provide expert advice and tools to put our safety policies into practice.

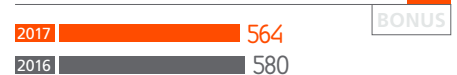
Some employees may be exposed to long-term health risks from hazardous substances and other physical hazards. We aim to reduce exposure levels to hazardous substances and to seek alternatives, where possible. We provide our employees with health surveillance to understand and reduce the impact of workplace health risks.

We use the Recordable Accident Rate as a key performance indicator to measure workplace injuries. This metric, along with the number of major injuries, is used to determine an element of executive bonus (see page 101). In 2017, there was a 3% reduction in the Recordable Accident Rate, a 28% reduction in the total number of major injuries recorded and no fatalities as we continued to focus on reducing risk and embedding safety culture to drive improvement.

2018 priorities

We will continue to drive towards a world-class level of safety performance; focus on the management and reduction of safety risk; and drive a strong safety culture through communication, awareness and visible leadership. We will target a 10% reduction in the Recordable Accident Rate.

Recordable Accident Rate (per 100,000 employees)²



Major injuries recorded^{2,3}



BONUS

5% of the UK executive directors' bonuses are based on the achievement of safety KPIs (see page 101).

1. Occupational Health and Safety Assessment Series.
2. See summary of Deloitte LLP assurance on page 65.
3. The definition of a major injury was updated in 2017 to more closely align with the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 2014.